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联合国粮食及农业组织

Food and Agriculture Organization of the United Nations

Organisation des Nations Unies pour l'alimentation et l'agriculture

Продовольственная и сельскохозяйственная организация Объединенных Наций

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CONFERENCE

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Audited Accounts – FAO 2008-2009 **Part B – Report of the External Auditor**

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REPORT OF THE EXTERNAL AUDITOR ON THE FINANCIAL STATEMENTS OF THE FOOD AND AGRICULTURE ORGANIZATION OF THE UNITED NATIONS FOR THE FINANCIAL PERIOD 1 JANUARY 2008 TO 31 DECEMBER 2009

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PART I

GENERAL

Introduction

1. This report is submitted in accordance with Article 12.9 of the Financial Regulations. It contains the results of the audit of the Food and Agriculture Organization (FAO) of the United Nations for the biennium 2008-2009. The audit was based on Financial Regulations 12.1 to 12.10 of the FAO and the additional Terms of Reference relative to External Audit which are appended to said Financial Regulations.

2. This report includes our observations on the Financial Statements of the FAO covering the biennium 2008-2009 which are reported in Part I of this report.

3. Aside from the FAO Headquarters, our audit also included the operations of five regional offices[1] and six country offices[2] and covered selected management issues and compliance with FAO rules and regulations.

4. In particular, we evaluated Staff Related Liabilities (SRL), Contributions, Host Country Agreements (HCA), Working Capital Fund (WCF), Budgetary Controls, Consultancy Contracts, Prepayments, Property Management, Procurement, Project Management and the Special Fund for Emergency and Rehabilitation Activities (SFERA).

5. Our observations on losses written off, ex-gratia payments and cases of fraud or presumptive fraud during the biennium are disclosed in Part IV of this Report.

6. This report also contains our recommendations to rectify the deficiencies noted and improve the operations. Following past practice, these recommendations are categorized as Fundamental, Significant and Meriting Attention[3].

Summary of Recommendations

	AUDIT OF HEADQUARTERS	Priority	Timeline
1	We strongly recommend that the Organization take the matter of funding its staff related liabilities with extreme urgency as deferment of decisions most particularly on funding proposals will in no doubt compromise the financial viability of the Programme of Work and Budget (PWB) in future years. (Paragraph 34)	Fundamental	2010

[1] Regional Office for Asia and the Pacific, Bangkok; Regional Office for Africa, Accra, Ghana; Regional Office for Europe and Central Asia, Budapest, Hungary; Regional Office for the Near East, Cairo, Egypt and Regional Office for Latin America and the Caribbean, Santiago, Chile.

[2] Country Offices for Cambodia, Burkina Faso, Turkey, Nigeria, Chile and Lao People's Democratic Republic.

[3] Fundamental: Action is considered imperative to ensure that the Organization is not exposed to high risks. Failure to take action could result in serious financial consequences and major operational disruptions.

Significant: Action is considered necessary to avoid exposure to significant risks. Failure to take action could result in financial consequences and operational disruption.

Merits Attention: Action is considered desirable and should result in enhanced control or better value for money.

2	We acknowledge Management's conformity with our recommendation and its extensive efforts to improve the timeliness of payment of contributions, including continual follow ups with governments on outstanding items, coordination with Field Offices on communication with governments on arrears in GCCC, and negotiation of instalments payment plans for those countries dealing with significant arrears. In addition, we acknowledge the consistent monthly reporting provided by management on the situation of contributions and arrears that is posted both on the external website and the website for Permanent Representations. (Paragraph 43)	Fundamental	2010
3	We recommended and the Organization agreed to undertake a comprehensive review of outdated Host Country Agreements (HCAs) to assess the adequacy of the contributions, in cash or in kind, and explore the possibility of generating additional revenues by negotiating improved cost-sharing schemes between the Organization and amenable host countries. (Paragraph 48)	Fundamental	2010
4	We recommended that the Organization seriously consider increasing the level of the Working Capital Fund (WCF) to provide sufficient buffer to the General Fund (GF). In this regard, the Secretariat confirmed that they will include proposals to increase the level of the WCF in the PWB for 2012-13 under the section on Financial Health similar to those which were previously presented in the PWB 2010-11 but which were not endorsed by the Membership at that time. We also reiterate our recommendation that the Organization continue its efforts to collect contributions and arrears due from member states. (Paragraph 56)	Fundamental	2010
5	We encourage the Organization to consider the standard Oracle budgetary functionality for effective and efficient fund sufficiency checking in accordance with the budget fungibility rules. (Paragraph 66)	Fundamental	2010
6	We recommend that the Organization review thoroughly the performance of the consultants and consider the non-reengagement of those who have not been able to meet the reporting requirements as contained in the contracts**.** The Organization agrees with the recommendation and notes that quality assessment document drafted by the hiring division shall indicate whether the established deadlines were not met and provide reasons why, and contain a statement of non-rehire if applicable. In this context, we were informed that forms aimed at standardizing Terms of Reference (TORs), objectives and expected outputs for Consultants and Personal Service agreements were transmitted throughout the Organization on 8 September 2010. (Paragraph 73)	Fundamental	2012
7	We recommend that the Organization examine more closely the causes of the delay in closure actions in	Fundamental	2011

	order to address them adequately and set a target of reduction of this delay. (Paragraph 88)		
8	We suggest that the Organization: a) in accordance with the principle of reasonable alignment of support costs to field programmes and projects as they had actually materialized and recoveries from donor funded projects, work on the immediate expansion of the policy on support cost reimbursements to include recovery of any fixed indirect costs as far as already acceptable to donors and can be made acceptable to them and provide for the appropriate guidelines and training required. b) in accordance with the principle of transparency and in order to accurately establish the reasonable level of support cost reimbursements, consider reporting and assessing the level of reimbursements of support costs from Extra Budgetary (EB) funded projects to show the following: b.1 unrecovered fixed indirect support costs; b.2 unrecovered support costs by category of programmes or projects; b.3 unrecovered support costs represented by the difference between the approved Technical Support Services (TSS) and Project Servicing Costs (PSC) rates and actual reimbursements; and b.4 unrecovered support costs represented by the difference between the support cost income budgeted and the actual reimbursements by manner of recovery (fixed-percentage charge, direct charge to programme or project or combination of the two). c) in order to present fairly the support costs actually incurred under the Regular Programme (RP) funds, consider the disclosure in the financial statements of the unrecovered support costs from donor funded projects and absorbed by the RP fund and how these were calculated. d) in keeping with the principle of reasonable alignment of support costs to field programmes and projects as they had actually materialized and recoveries from donor funded projects, and in order to accurately establish the reasonable level of TSS cost recovery: d.1 consider articulating the instances where recovery is possible or not; and d.2 establish the extent at which the Organization desires to recover the cost of TSS. (Paragraph 106)	Fundamental	2012

9	We recommend that issuances of property to a staff member be documented by a Custody of Property Form and that the listing of properties in the name of the division be used only for common equipment such as printers, and photocopiers or divisional (shared) laptops. We also suggest that staff members be required to secure gate passes before a property item is taken out of office premises. (Paragraph 113)	Fundamental	2010
10	We recommend that the Organization revisit its policies and procedures in the recognition of non-expendable property and that the valuation method used in recognizing non-expendable property as purchases and as inventory are consistent**.** (Paragraph 122)	Fundamental	2010
11	We recognize that the Organization is revising its asset management policies and procedures within IPSAS and recommend that the Organization ensure that the submission of Year End Asset Report (YEAR) by the Offices outside Headquarters as to the timeline of submission, the monitoring of their submission and the immediate verification and reconciliation of property records in the Organization is included in the new policy. (Paragraph 130)	Fundamental	2011-12
12	We were informed of the improvements made in the policies related to the recovery of tax advances. However, we still recommend that the Organization through its Liaison Office in Washington require the strict enforcement of the submission of the annual tax returns within the deadline set in the Administrative Circular AC2010/08 so that prepayments are promptly cleared and excess advances refunded immediately by the staff members. (Paragraph 135)	Significant	2012
13	We emphasize the importance of an intensive monitoring effort and the importance of ensuring the timely settlement of advances especially those remaining uncleared beyond the prescriptive period and that the grant of advances for OCAs be limited to the restrictions of DGP064 so as not to unduly burden the consultants and allow for the immediate settlement of the said advances. (Paragraph 143)	Significant	2012
14	We recommend that the Organization sustain its efforts to collect the remaining payroll writebacks. (Paragraph 146)	Significant	2012
15	We recommend that the Organization implement Technical Cooperation Programme (TCP) projects within the terms of the existing UN Financial Regulation 4.3, specifically the cancellation of unutilized appropriation at the close of the financial period for which the appropriation was voted for to ensure proper programming and implementation of project activities within their approved budgets and appropriation for the year/biennium. (Paragraph 151)	Significant	2012
16	We recommend that the Organization consider placing the	Significant	2012

	earmarked long term investment and advance payments for the Separation Payment Schemes (SPS) in a separate trust fund to properly recognize them as Plan Assets as part of the effort towards full adoption of International Public Sector Accounting Standards (IPSAS). (Paragraph 157)		
17	We recommend that the monitoring of deliveries be strictly performed by the Budget Holders (BH). The recommendation to impose penalties, if any, should be made by him/her already and subsequently deducted from the payment. (Paragraph 162)	Significant	2011 onwards
18	We recommend that the Organization set a policy that will hold the traveller accountable for the cost of tickets, surcharges and fees where cancellations are caused by him without justifiable reasons. The Organization noted that it will review the impact of such a policy within the context of the staff rules. Simultaneously a communication strategy will be undertaken to sensitize budget holders and approvers of cancellations charges to the cost of cancellation and the need to determine upfront the validity of these charges. (Paragraph 166)	Merits Attention	2012
19	We recommend that management pursue the formulation of guidelines for the SFERA that will specify the maximum amount of the advances that may be granted to a specific project and the definite period within which said advance will be recovered. (Paragraph 175)	Merits Attention	2012
	AUDIT OF DECENTRALIZED OFFICES		
20	We recommend that the Regional Office for Africa (RAF) enforce more strictly the requirement to secure prior approval from the Office of Strategy, Planning and Resources Management (OSP) before incurring commitments and expenditures requiring shifts of allotments exceeding USD 100,000 at programme level and USD 20,000 each at chapter and allottee levels. RAF's request for shift, which may be included in the PBR, needs to state specifically the allotted amounts to be shifted, the source of allotment for transfer between programmes or chapters and the reasons or justifications for the transfer. We also encourage RAF to work consistently within the limit of the institutional allotment provided in accordance with the PWB. (Paragraph 181)	Fundamental	2010
21	We recommended and RAF agreed that the Budget Holders (BHs) endeavour to work within the approved project budget for TCP and in the case of Trust Fund (TF) project within the cash received from donor. To ensure that funds are available for the project before incurring commitments and expenditures, the BH should consider employing worksheet of actual commitments and expenditures outside of the existing systems to keep track of project cash or fund balance until system embedded controls to prevent over-expenditure are put in place.	Fundamental	2010

	In the event that the cash balance is low and there is a need to obtain additional cash from the donor and as required in the Project Agreement, the BH needs to promptly request from the Finance Division - Project Accounting (CSFE) the need for the Call for Funds and submit budget revision needing donor's consent/approval to prevent incurrence of negative cash balance for TF projects. (Paragraph 187)		
22	We recommend the (i) intensified review of accounting transactions; (ii) periodic and up-to-date reconciliation of the inventory records between the decentralized offices and the headquarters; and (iii) preparation and timely submission of ADM 41 and ADM 83**.** (Paragraph 192)	Fundamental	2010
23	We recommended and management issued guidelines and a standard template including the TOR of each contract that define (i) tangible and measurable outputs of the work assignment; (ii) deadlines for delivery of outputs and details as to how the work must be delivered, and (iii) performance indicators among others. We further recommend that the TOR be linked by clear reference (i.e., Annex) as integral part to the agreement and we appreciate management's plan to integrate the same as part of the PSA. (Paragraph 202)	Fundamental	2011
24	While we appreciate the effort of the Organization to prevent the accumulation and further reduce outstanding travel advances, relevant offices should coordinate with Human Resource (HR) Services and Travel Incoming-TECs, Budapest for the follow-up and collection of advances from ex-consultants who were already paid of final honoraria. We also recommend that the Organization include in the consultant's TOR the requirement on submission of TEC and the recovery of outstanding travel advance on the payment of final honorarium. (Paragraph 208)	Fundamental	2011
25	We reiterate that utmost efforts be exerted to observe the timelines for project implementation and completion. (Paragraph 214)	Fundamental	2011
26	We recommend that the FAO Representation in Laos (i) allocate the necessary budget for overtime services when preparing budget estimates; (ii) ensure the availability of funds before payments thereof; and (iii) use the appropriate accounts in recording such payments. (Paragraph 218)	Fundamental	2012
27	We recommend that Decentralized Offices consider implementation of requirement that the specific delivery dates be disclosed in the Purchase Orders (PO) that will be served to the vendors and to which the vendors should agree. (Paragraph 224)	Significant	2011

Audit of Financial Statements

7. The audit of financial statements was carried out in conformity with the International Standards of Auditing. These standards require that the audit be planned and carried out to obtain reasonable assurance that the financial statements are free from material misstatements. The Organization is responsible for the preparation of the financial statements. Our responsibility is to express an opinion on them.

8. The audit included examining, on a test basis, evidences supporting the amounts and disclosures in the financial statements. It also included the assessment of the accounting principles used and significant estimates made by the Organization, as well as evaluating the overall presentation of the financial statements.

9. Furthermore, we were requested to perform the audit of the following separate financial statements for the programmes implemented in cooperation with or on behalf other agencies, namely:

- FAO/UN Population Fund (UNFPA) Biennium Status of Funds and Schedule I – Biennial Expenditures Statement as at 31 December 2009;
- FAO/United Nations Development Programme (UNDP) Status of Funds and Schedule I – Schedule of Expenditures on Projects executed by FAO, as at 31 December 2009; and
- FAO/Global Environment Facility Fund (GEF) – Status of Funds for the biennium ended 31 December 2009.

10. The audit enabled us to issue an unqualified audit opinion on the financial statements of the Food and Agriculture Organization of the United Nations for the biennium 2008-2009.

Previous Recommendations

11. We have not separately included comments on the actions taken on the previous recommendations except when the context demanded so as the Finance Committee (FC) had already developed a mechanism of following up all previous recommendations the Organization has yet to fully address.

FINANCIAL MATTERS

Financial Position of the Organization

12. The financial position of the Organization significantly declined during the biennium 2008-2009. From a net shortfall of income over expenditures in the General and Related Funds in the previous biennium of USD 55.21 million, the shortfall had increased to USD 100.37 million for this biennium. The increment of USD 45.16 million represents an 81.8 per cent rise over that of 2006-2007. Accounting for a major portion for the increase in shortfall was the interest cost of staff related liabilities which amounted to USD 94.75 million.

13. Overall, the negative fund balance at the end of the biennium further dipped to USD 558.99 million from USD 465.28 million in 2006-2007.

14. As regards the Trust and UNDP Funds, the Organization had an excess of income over expenditures of USD 5.49 million which was also transferred to donor accounts, thus leaving the Fund balance unchanged at the end of the period.

15. The assets of the FAO under the General and Related Funds totalled USD 461.32 million as at 31 December 2009 against USD 488.86 million as at 31 December 2007. Cash and term deposits increased from USD 36.20 million to USD 55.41 million (53.10 per cent) while Contributions Receivable decreased from USD 122.29 million to USD 82.39 million (32.63 per cent).

16. On the other hand, liabilities increased from USD 867.93 million as at 31 December 2007 to USD 934.35 million as at 31 December 2009 representing an increment of USD 66.42 million. The increase was due to the hike in Contributions received in advance, unliquidated obligations and Staff Related Liabilities (SRLs). It may also be noted that in December 2008, the Organization borrowed USD 25 million to meet operating costs (see paragraph 51).

17. The deficit in Reserves and Fund Balances continued to increase – rising from USD 379.08 million to USD 473.03 million representing an increase of USD 93.95 million or 24.78 per cent.

18. Under the Trust and UNDP Funds, assets grew by USD 240.02 million, that is, from USD 669.84 million to USD 909.86 million. The liabilities also increased by USD 229.62 million, that is, from USD 646.77 million to USD 876.39 million. Total fund reserves and fund balances amounted to USD 33.48 million as at 31 December 2009, exceeding the 31 December 2007 balance of USD 23.08 million.

19. The under funding of staff related liabilities continues to be a cause of structural deficit in the General Fund. The total liability for the four plans at 31 December 2009 was USD 1,110.9 million of which USD 806.0 million was unfunded.

Liquidity Position

20. The current ratio of the Organization as of 31 December 2009 was 1.05, which is below that of the 2006-2007 biennium of 1.08. Although there was a slight increase in the current asset balance, the increment in current liabilities was bigger thereby resulting in the lower current asset ratio.

21. There is a noticeable decrease in outstanding assessed contributions. Comparison of the biennium end figures would show that from 2006-2007 balance of USD 113.18 million, the balance went down to USD 75.58 million.

22. As in the previous years, staff salaries continued to form a major part of the Organization's expenses. For 2008-2009 staff salaries for the General and Related Funds amounted to USD 630 million or 60 per cent of the total expenditures, while for Trust and UNDP Funds, the same totalled USD 200 million or 18 per cent of the total expenditures. It may be added that equipment purchases of USD 327 million or 29 per cent comprised the biggest chunk of expenditures for Trust and UNDP Funds.

PART II

AUDIT OF HEADQUARTERS

Staff Related Liabilities

23. Our audit of Staff Related Liabilities (SRL) showed that the last valuation thereof was contained in the 31 December 2009 Actuarial Valuation Report. The total actuarial liability amounted to USD 1,110.80 million and consisted of USD 18 million for Compensation Plan Reserve Fund (CPRF); USD 58.20 million for Termination Payments Fund (TPF); USD 100.10 million for Separation Payment Scheme (SPS); and USD 934.50 million for After Service Medical Coverage (ASMC). It is worthy to mention that the balance of SRL increased by USD 391.70 million (or 54.47 per cent) from the 2007 balance of USD 719.10 million with the increment in ASMC of USD 358.40 million, accounting for 91 per cent of the increase.

24. With regard to the funding of the SRL, Conference Resolutions 10/99 and 10/2001 provided that long-term investments and any income which they generate are to be applied first to ensure the adequacy of funding of the SPS and CPRF, and that any additional investments and related income then be earmarked for the ASMC and subsequently for the TPF.

25. In 2003, the Conference agreed to begin funding the liability towards past-service ASMC through additional assessment of USD 14.1 million beginning with the biennium 2004-2005. The Secretariat has highlighted the inadequacy of the current biennial funding plan, considering the scale of the liability, in its reports to the Governing Bodies in past years which have stressed the importance of full funding of both the ASMC and TPF past service liabilities.

26. In our audits, we brought to the attention of the Organization the precarious financial condition that it was in, brought about by the underfunding of ASMC and TPF. The debt ratio, which was determined to be more than one (1) was discouraging as it signified that there were lesser assets that were available to pay for FAO's debts. This lamentable condition persisted despite the infusion of additional contributions amounting to USD 14.1 million by the Member Nations pursuant to the Conference Resolution.

27. The required annual amortization to fund the ASMC is USD 24.8 million with which it would take 30 years or until 2040 to fully fund ASMC's past service liability. Of this amount, however, only USD 7.05 million or 28 per cent was appropriated in the PWB resulting in a funding shortfall of USD 17.8 million for 2009.

28. The predicament of the Organization concerning TPF offered no reason for optimism either as the total past service liability remained unfunded since no funding source had ever been approved for the past service liabililty related to this plan. Cash outflows in excess of the funding provided for TPF current service costs therefore generate a structural cash deficit in the General Fund. During the financial period 2008-2009, the Organization paid TPF amounting to USD 22.27 million, which payment contributed further to the structural cash deficit in the GF of the Organization to the extent that it exceeded the current service funding for these liabilities during the biennium.

29. In addition to inadequate funding of the plans, the Organization cannot rely entirely on the income generated from the long term investments in a 50 per cent equity and a 50 per cent fixed income/bonds because these investments are market driven and therefore subject to a high degree of instability. In 2008, global financial markets suffered from extreme levels of volatility and tight credit not seen in decades. In 2009, despite initial signs of recovery, these investments particularly in equity incurred a net loss as at the end of the financial period.

30. The impact of the market conditions as stated above further contributed to the inadequacy of the investment funding. Due to this inadequacy of funding, the value of investments is significantly less than the present value of liabilities and the growth in the latter will always outpace that of the former unless an improved funding strategy is adopted.

31. The Secretariat, based on FC guidance, made proposals for funding the ASMC and TPF within the context of the Programme of Work and Budget 2010-11. The Conference decided not to approve any additional contributions, thus necessitating a deferral of any potential funding increases to the next PWB for the 2012-13 biennium.

32. The FC in its 132nd session fittingly paid attention to the seriousness of the underfunded ASMC liability and the unfunded TPF. Acknowledging the challenges in containing the growth in the liabilities and in the ratio of retirees to active staff member, the Committee, decided to wait for the 2010 actuarial valuation of SRL to make funding recommendations to the Council in the context of the PWB 2012-13.

33. The shortfalls in the annual funding of ASMC noted above will further inflate the huge net deficit that the Organization is already facing. The increasing deficits in biennia 2004-2005, 2006-2007 and 2008-2009 of USD 103.61 million, USD 356.00 million and USD 439.55 million, respectively, and the unfavorable debt-equity ratio undermine the Organization’s financial position which will translate into higher risks to its stakeholders, the Member Nations and donors.

34. We strongly recommend that the Organization take the matter of funding its staff related liabilities with extreme urgency as deferment of decisions most particularly on funding proposals will in no doubt compromise the financial viability of the PWB in future years.

Delayed payments of contributions

35. The Organization’s appropriations for a financial period are financed by annual contributions from Member Nations and Associate Members. In December of each year, the Organization bills each member for (a) the full amount of the contributions of the following year; (b) any replenishment of the Working Capital Fund (WCF) and Special Reserve Account (SRA) in accordance with the level of reassessment as determined by the FAO Conference; and (c) the share of the governmental counterparts in the operating costs of the FAO office in their respective countries as agreed upon.

36. Financial Regulation 5.5 requires that contributions and advances shall be due and payable in full within 30 days of the receipt of the communication of the Director-General or as of the first day of the calendar year to which they relate, whichever is later. As of 1

January of the following calendar year, the unpaid balance of such contributions and advances shall be considered to be one year in arrears.

37. As at 31 December 2009, Contributions Receivable Account (Account 1021) had an outstanding balance of USD 82,391,039.64, which is 17.86 per cent of total assets of USD 461,318,000.00. The balance is broken down as follows:

Account Title	Account Code	Amount (In USD)	%
Assessments	2600	75,581,243.39	91.74
Government Counterpart Cash Contributions	2601	4,397,072.05	5.33
Working Capital Fund	2602	62,475.00	0.08
Special Reserve Account	2603	2,350,249.20	2.85
Total		82,391,039.64	100.00

38. The receivables on Assessments consisted of the assessments for the current year totalling USD 45.83 million and those of prior years' (arrears) of USD 29.75 million which was about 40 per cent of the account balance. The arrears comprised of unpaid assessed contributions of 46 Member Nations and of which USD 23.08 million had been uncollected for more than four years.

39. Similarly, USD 3.168 million or 72 per cent of the receivables on Government Counterpart Cash Contributions (GCCC) remained outstanding for five to twenty years already. For receivables on WCF, an uncollected amount of USD 54,475 or 87 per cent of the total WCF balance, and the entire receivables for the SRA of USD 2.350 million had been outstanding for more than 15 years.

40. We express our concern for the delayed payment by Member Nations of assessed contributions due from them since this undermines the Organization's liquidity. This holds true also for the non-payment of arrears in Contributions Receivables for Assessments, GCCC, WCF and SRA. Due to delays in the receipt of contributions from Members, the entire WCF balance amounting to USD 25,653,558.50 was advanced to the GF in December 2008 to meet the operational requirements of the RP. The liquidity problem caused by the poor timing of Members' payments of their assessed contributions also obliged the Organization to resort to external borrowings ranging from USD 10 million to USD 15 million in December 2008 and in January 2009 to meet operating costs.

41. Funds tied up in overdue receivables weigh heavily on the Organization's liquidity levels and may preclude an efficient and timely implementation of FAO's Regular Programme (RP).

42. While we noted the diligent efforts being taken by the Organization to encourage the payment of assessed contributions on a timely basis, we believe that sufficient efforts should also be undertaken for the collection of long outstanding accounts (arrears) which

have already totalled USD 29.66 million or 36 per cent of the total receivables as of December 2009.

43. We acknowledge Management's conformity with our recommendation and its extensive efforts to improve the timeliness of payment of contributions, including continual follow ups with governments on outstanding items, coordination with Field Offices on communication with governments on arrears in GCCC, and negotiation of instalments payment plans for those countries dealing with significant arrears. In addition, we acknowledge the consistent monthly reporting provided by management on the situation of contributions and arrears that is posted both on the external website and the website for Permanent Representations.

Host Country Agreements

44. FAO's presence in the different countries is manifested in its local offices called Representations and to support these Representations, the Organization allocates funds for their operations. In 2009, total allocations amounted to USD 49.53 million. In addition, the FAO bills the host Governments for part of the operating costs based on the agreements known as Host Country Agreements (HCA) and the collectibles are recorded in the Headquarters under Receivables – GCCC. For 2009, total billings made to 37 out of 136 Representations amounted to USD 870,000. For the 99 countries not billed, there were no agreements regarding cash contributions but instead contributions in kind such as free use of office premises and provision of office furniture and equipment, among others would be extended.

45. We noted that the billings were correctly made. Our perusal of the HCA for the countries billed disclosed that 23 of the 37 HCA were forged in the 70s, 9 in the 80s, 3 in the 90s and the rest in the year 2000 and up. While the HCA generally stipulate that these be subject to periodic reviews and re-negotiation, it was evident that majority of the agreements, having been signed 40 years ago, had become outdated especially in terms of the amounts to be billed to the Representations. The contributions might have been substantial at the time when the agreements were originally made but had obviously been rendered less consequential by the passage of time.

46. When viewed against the budgets allocated by FAO, the amounts of collectibles from 21 Representations whose HCA were forged in the 70s, accounted for only 0.02 per cent to 26.29 per cent. Only in two instances did these billings reach 50 per cent or more of the FAO allocations. For three HCA made in the 90's, the billings were 50 per cent, 92 per cent and 9 per cent of the respective FAO country budgets.

47. In addition to the cash contributions, we recognize the merits of contributions in kind, which host countries provide consistent with HCA, which, however, were not assigned values and are not recognized in the books by the Organization.

48. We recommended and management agreed to undertake a comprehensive review of outdated HCAs to assess the adequacy of the contributions, in cash or in kind, and explore the possibility of generating additional revenues by negotiating improved cost-sharing schemes between the Organization and amenable host countries. It further added that after receiving inputs from the Regional Conferences, the Organization is to formulate and present to the relevant Governing Bodies for review and approval,

proposals for a medium to long-term vision of FAO coverage, in accordance with the decision of the FAO Conference of November 2009.

Working Capital Fund

49. The Working Capital Fund (WCF) is established and governed by Financial Regulations 6.2 to 6.6. The authorized level of the WCF has been revised several times by Conference. The last update to the authorized level of the WCF was made by Conference Resolution 15/91, adopted on 26 November 1991, which established a level of USD 25 million. Since then, there has been no major augmentation of the Fund through reassessment of members and as at 31 December 2009, it is at a level of USD 25,653,558.50.

50. Financial Regulation VI.2 provides that the WCF is maintained for the primary purpose of advancing monies, on a reimbursable basis, to the General Fund (GF) to finance expenditures in the implementation of the Regular Programme, pending receipt of assessed contributions from member countries. The WCF may also be used to finance emergency expenditures not provided for in the current budget and for making loans for purposes as the Council may authorize in specific cases.

51. We analyzed the movements of the WCF from 1 January 2005 to 31 December 2009 to determine the fund's adequacy to temporarily answer for operational needs of the General Fund in the event of delays in the collection of members' assessed contributions to the regular budget. Although the amounts advanced were subsequently reimbursed by the GF to the WCF, we noted that the WCF hit critical levels and was practically depleted as at several dates. As at 31 December 2005, WCF had a balance of only USD 18.00 which was .00007 per cent of the authorized WCF level. The Fund was also at an unfavorable level as at the end of 2006 at only USD 276,536.50, or 1.09 per cent of the authorized level, due to advances by the GF which remained not reimbursed as at year end. This level was also hit in 2008 in which the balance was only USD 36.40 at the end of the year, which is 0.00014 per cent of the WCF authorized level.

52. As revealed in audit, the borrowings from the WCF by the GF were necessitated by the delayed and poor timing of payment of assessed contributions from member nations. (Please refer to the discussions on delayed payment of contributions.)

53. We also scrutinized the monthly cash position vis-a-vis the monthly operational cash requirements from 2007 to 2009 which is USD 38 million on the average. Results of our analysis showed the inadequacy of the WCF to provide a buffer for the GF in the meantime that assessed contributions remained not fully collected. Notably, even after advancing the full amount of the WCF to the GF, cash deficit still resulted.

54. The cash shortfalls triggered external borrowings. Available loan data showed that the Organization had to resort to extensive periods of external borrowing in 2006 which reached a peak of USD 104 million. Again in 2007, external borrowing was required but for shorter periods and smaller amounts, with a peak of USD 25 million. Total borrowing costs for 2006-2007 were USD 1.8 million (2004-2005 totalled USD 3 million) of which USD 1.5 million was incurred in 2006. In December 2008, two external loans were obtained so as to meet operating costs, in the amounts of USD 10 million and USD 15 million.

55. We are concerned that the sustained periods of external borrowings triggered by liquidity shortfalls, following full utilization of the WCF, indicate the inadequacy of the current authorized level of the WCF to serve the primary purpose for which it was established. In more precise terms, the current WCF level of USD 25,653,558.50 is not sufficient to temporarily answer for expenditures in the implementation of the Regular Programme, pending receipt of assessed contributions from member countries without recourse to borrowing. The level of the WCF, which was decided by the Conference 18 years ago, no longer provides an adequate safety net to prevent recourse to external borrowing and should be reviewed in the light of the Organization's current operational cash requirements.

56. We recommended that the Organization seriously consider increasing the level of the WCF to provide sufficient buffer to the GF. In this regard, the Secretariat confirmed that they will include proposals to increase the level of the WCF in the PWB for 2012-13 under the section on Financial Health similar to those which were previously presented in the PWB 2010-11 but which were not endorsed by the Membership at that time. We also reiterate our recommendation that the Organization continue its efforts to correct contributions and arrearages due from member states.

Regular Programme Budgetary Controls

57. Inquiry disclosed that Oracle standard budget functionality relating to fund sufficiency was not activated because it could not meet the budget fungibility requirements of the Organization. As such, the main control over the proper use of Organization fund lies with the certification process entrusted to designated Budget Holders (BHs). The BH is then responsible for the monitoring, control and reporting of the budgets under the overall supervision of the department head or the allottee.

58. In the absence of funds sufficiency checking at Oracle financials, we noted instances wherein allotments for a given programme, programme entity or division had been exceeded by the total commitments and actual expenditures by the budget holders and allottees. These over-expenditures in some programmes had to be balanced by under-expenditures in other programmes and could have significant impact on the implementation of affected programmes. The absence of sufficiency checking also allowed the incurrence of commitments and expenditures under obsolete programme entity and activity codes. While the Office of Strategy Planning and Resources Management (OSP) would detect or be informed of these occurrences through the Periodic Budgetary Performance Reports (PBRs) submitted on a quarterly basis, the overruns had already been committed before approval/clearance of amendment to allotment or budgetary transfers could be done or implemented by the OSP. Errors resulting from charging of commitments and expenditures to invalid codes would necessitate journal voucher preparation.

59. We are concerned that no controls are embedded in the existing applications systems that will prevent incurrence of expenditures and commitments that are contrary to the budget fungibility rules when BH are committing funds against allotments. For example, an absolute fund checking on allotment for hospitality account will prevent the BH from incurring commitments in excess of allotments. On the other hand, an advisory funds checking level will advise the BH when a transaction fails fund checking.

Moreover, in manual controls employed by the BH the consistency in the application of budgetary control may not be assured.

60. OSP and the Finance Division (CSF) stated that past practice showed that the number of errors, where allottees have to take the corrective measures is minimal whereas overruns at the institutional allotment level for the most part result in allotment adjustments requests to OSP, realigning planned budgets to the pace of implementation or emerging issues. Allottees are required to explain such transfers providing valuable insights on the FAO implementation work and subsequent planning cycles.

61. Given the above, OSP and CSF emphasized its approach to budgetary control has been to ensure that budget holders are provided with regularly updated budget status information which includes all transactions processed in both Oracle and non-Oracle applications. Such information is made available to BHs via the Oracle Data Warehouse (ODW) and is updated on a daily basis. BHs are instructed to review this information regularly and to commit funds after review of the available balances. In addition to this, the Organization has established systems and procedures for monitoring and reporting on the status of allottee appropriations and for the review and authorization of additions to and transfers between allotments.

62. We took note of the comments of the OSP relating to the controls undertaken which are detective and not systems based. We also recognized that funds sufficiency checking may not be undertaken for transactions coming from the Oracle payroll system and other feeder systems.

63. It cannot be denied that activation of the budgetary functionality in Oracle financial modules shall ensure that balances of allotments pertaining to certain programme entity, division or department would be updated once commitment and expenditures are entered in any Oracle module. This can be used to validate funds sufficiency for commitments being raised by the budget holders, say in Oracle Purchasing (OP) module, for a given programme entity/division/department without going to the reports in the DW. As such, incurrence of commitments and expenditures contrary to budget fungibility rules will be prevented in a consistent and timely manner.

64. Our audit of Regional Office (RO) disclosed that for one office at the end of 2009 its expenditures exceeded the allotments by USD 170,000 (excluding standard/staff cost variance). The justification offered by the regional office that the Oracle financials did not prevent them from incurring commitments and expenditures beyond the allowed budget flexibility clearly demonstrated the insufficient fund checking functionality of Oracle financials.

65. The comments that BHs are provided with regularly updated budget status information including all transactions processed in both Oracle and non-Oracle applications, made available to them via ODW and updated on a daily basis were negated by the fact that in the said RO expenditures exceeded the allotments in two chapters from 12 to 138 per cent. The same happened in ten programmes with the excess ranging from 34 to 632 per cent.

66. We encourage the Organization, whenever practicable, to consider the standard Oracle budgetary functionality for efficient and effective fund sufficiency checking in accordance with the budget fungibility rules.

Consultant Contracts' terms of reference and outputs

67. We brought to the attention of the Organization the absence of guidelines on the formulation of the Terms of Reference (TORs) for consultancy contracts that should include requirements that the outputs of the work assignment are tangible and measurable, delivery dates are realistic and details as to how the work must be delivered are described. We noted with concern that in a review of sampled 40 consultancy contracts 28 TORs did not define what has to be achieved out of the engagement; 31 did not provide details as to how the output must be delivered; 16 did not specify the dates when the output shall be achieved; and 33 had no performance indicators for an objective evaluation. Finally, six contracts were not supported with TOR.

68. We appreciate management's compliance with our recommendation for the formulation the TOR that would address the noted deficiencies thru its issuance of a template for non-staff human resources consisting of three main sections and for immediate implementation.

69. Our audit also showed that in 16 of the 30 contracts, the consultants were unable to submit their final outputs at the agreed time with the delays running to as much as 15 weeks. In addition to them, it was also observed that two experts were unable to complete their assignments due to health reasons, one consultant abandoned the mission and two submitted incomplete or unsatisfactory reports as evaluated by the Lead Technical Unit (LTU).

70. Likewise, of the 30 contracts reviewed, 12 were extension contracts for which only two reports were submitted before the end of the engagements, eight reports were submitted beyond Not to Exceed (NTE) dates and two reports were not submitted at all.

71. Although management justified that the concerned divisions conducted follow ups on the submission of reports, meetings with the consultants, direct backstopping of the work, evaluation of the work plans and review of TORs, we believe that the same had not been enough to compel the consultants to comply with the requirements on the timely submission of outputs. In particular we want to point out the fact that the reports for extension contracts could have been completed earlier or at the time the extended contracts expired as these covered only a prolonged period. Unfortunately, as discussed before only two of the twelve reports were submitted on time.

72. While the consultants were not paid their final honoraria pending completion and delivery of satisfactory work, the delays in reporting are detrimental to the project. It bears stressing that consultants are recruited primarily to provide immediate and desired inputs for use within the RP and EB funded assignments/projects.

73. We recommend that the Organization review thoroughly the performance of the consultants and consider the non-reengagement of those who have not been able to meet the reporting requirements as contained in the contracts**.** The Organization agrees with the recommendation and notes that quality assessment document drafted by the hiring

division shall indicate whether the established deadlines were not met and provide reasons why, and contain a statement of non-rehire if applicable. In this context, we were informed that forms aimed at standardizing Terms of Reference (TORs), objectives and expected outputs for Consultants and Personal Service agreements were transmitted throughout the Organization on 8 September 2010.

Project Management – Project Closure

74. We reviewed project closure activities from the dates by which field activities must be completed at the project sites or Not to Exceed (NTE) dates to operational and financial closures aimed at determining whether the required activities were completed in a timely manner. Projects pending financial closure were downloaded from Field Programme Management Information System (FPMIS) and 361 projects that were operationally closed as at 31 December 2009 were filtered. In the process, we analyzed the lead time or time lags (in months) from NTE to operational closure and from operational closure to 30 April 2010. Financially closed projects were excluded because it is in the operationally closed projects that necessary measures may still be made to manage delay, if any.

75. Our audit showed that, on the average, it took 22 and 13 months for Technical Cooperation and Emergency projects, respectively, to be operationally closed from their NTE dates. In addition, the average lead times between operational closure and 30 April 2010 were 28 months for Technical cooperation and 18 months for Emergency projects. We are concerned of the considerable lead times as these are indicative of delay which may have a monetary effect and in terms of non-timely realisation of benefits or inputs to policies (project output, e.g. terminal reports transmitted to governments).

76. Among the 61 projects operationally closed in 2008, one (DJI/98/004/ /01/12) had its activities already completed in October 1999. This meant that it took 101 months for the Office to finalize the operational closure. There were also seven other projects (BDI/96/001/ /09/12, EP/RAF/102/GEF, UNTS/MAG/001/GEF, BKF/98/006/ /01/12, NER/01/004/ /08/12, NER/97/003/ /09/12 and BDI/02/006/ /01/12) that were operationally closed after a lapse of 45 to 82 days from the NTE. For those operationally closed in 2009, one project, GCP/INT/609/DEN became operationally closed 114 months after its NTE of September 1999.

77. The delays can be traced to the time spent in completing the following activities which are required before the project budget holder requests for such closure:

a) completion of all field personnel assignments;
b) fulfilment of contractual obligations by all sub-contractors;
c) delivery and, if appropriate, installation of the last major item of equipment;
d) disposal of all vehicles, equipment and supplies procured for the project;
e) award of all fellowships; and
f) completion of all reporting obligations, in particular, terminal reporting (Field Programme Circular (FPC) 2003/4, para. 4.9).

78. On project closure, the FAO TCP Guidelines, in particular, require that, once the project activities have been completed, the budget holder takes appropriate steps to close the project following established procedures governing project closure and any unspent

funds will be returned to the TCP General Account and reallocated to new projects (FAO TCP Guidelines, para. 58).

79. A project is financially closed once the operational closure has been confirmed and when no more charges are expected. Financial closure is effected by CSF once all the necessary criteria have been met. After financial closure, the project's accounts are closed and no charges can be made against them (FPC 2003/4, para. 4.9). Between operational closure to financial closure the main activities left are the following:

a) review and clearance of the terminal reports (unless not required) by the Reports Group, Resource Mobilization and Operation Service (TCSR, previously TCDM) for technical cooperation projects, Emergency Operation and Rehabilitation Division (TCE); Lead Technical Unit (LTU) at Headquarters or in Regional/Subregional Offices;
b) preparation of the final copy by TCSR and TCE;
c) transmittal of terminal reports to the government authorities of the recipient and/or donor countries;
d) budget equalisation, final budget revision (UNDP) or closing revision (TCP within 60 days after the latest approved NTE date) by the relevant TC funding liaison unit, either with or without prior consultation with or approval by the donor depending on the funding agreement and, in the case of Unilateral Trust Fund projects, submitted to the donor/recipient government for approval (FPC 2003/02, paras. 4.1.4 to 4.1.7); and
e) settlement of all remaining financial obligations of the project (FPC 2003/04, para. 4.4).

80. Of the 361 projects selected among projects not yet financially closed 91 had been operationally closed before 2008. We are concerned about the time lag between operational and financial closure.

81. We observed that the delays were evident in the review and clearance of reports. Based on the statistics as of 26 April 2010 as provided by the TCSR, out of the 532 reports received 50 have not been submitted to the Governments concerned. For the Terminal Reports/Statements of 2008-2010, out of the 356 reports received by the TCSR 84 have not been submitted. It may be added that on the average, the projects closed in 2009 had passed the NTE noted in FPMIS by 22 months and the latter by 48 months.

82. Management informed us that with regard to the final budget revisions of TCP projects the same have not been performed for those approved against the 2006-07 and 2008-09 biennia. Instead, the budgets are equalized to expenditure by CSF when the financial closure form is submitted by the BH or at the closure of the biennium, whichever comes first. For all TF projects, the financial closure can be requested by the BH and initiated when operational closure had been confirmed and no more charges are expected. The actual financial closure can only be performed in the corporate systems, however, when (a) financial reporting has been sent, including request for refund instructions; and (b) payment of remaining balance, refund or final payment has been made/received.

83. Management further explained that the financial closure in Oracle is completed after the completion of the first step while financial closure in FPMIS is completed after

the second step. In this context, an important factor for the delay in financial closure in FPMIS is, therefore, the time lag between the date of final financial reporting and the receipt of funds from the donor or donor's confirmation of refund instructions. The Organization has recently updated the procedure such that financial closure of the project is performed in FPMIS also after the initial step in those cases where no payment is expected from the donor.

84. Management also noted that TC sends automated messages (called triggers) on a monthly basis to budget holders (with copies to the Senior Field Programme Officer or SFPO) to remind them of the need to close projects. These messages are sent at least six months prior to NTE for TF projects and three months for TCP projects. Thereafter, they are sent on a monthly basis. The messages are available under each project (copies of messages sent prior to July 2009 can be availed if required). These automatic messages will also now be complemented on a more regular basis by the in-depth monitoring of project status performed by regional and subregional operations staff.

85. In the previous interim audits, we were informed that the causes of delay are non-regular submission of field programme/project narrative reports which are listed below. These causes had not been adequately addressed yet since, as discussed above the delays in the review and clearance of reports remain significant.

a) report not meeting the standard requirements/quality or missing information (e.g. recommendations for follow up, mandatory appendices, etc);
b) staff turnover;
c) draft report not being received on time from the field;
d) translation being required into different languages (in case of multiple recipients in English, French and Spanish);
e) workload of responsible persons at field and HQ levels;
f) funds not available/approved; and
g) users view the report as not responsive to the work requirements.

86. In an earlier observation issued regarding delays on terminal/final reporting, TCE pointed out that for emergency projects whose lifetime may be less than either four or six months, the timelines for reporting was unrealistic. Reports on Emergency projects are prepared as close as possible to the NTE and include technical and operational clearance. TCE keeps monitoring tables on "Activities Completed" projects and follows up with officers on a monthly basis – even prior to receipt of a follow-up message. There may also be occasional slippage in the updating of FPMIS data, and thus some reports which appear as "outstanding" are in fact completed.

87. Management is aware of the problem with delays in project closure and has taken some steps to improve the situation; we note that the closure of projects in Oracle and FPMIS has now been harmonized which will reduce the delays in financial closures. We feel however that further action is required to address the long standing problem regarding the timeliness of project closure.

88. We recommend that the Organization examine more closely the causes of the delay in closure actions in order to address them adequately and set a target of reduction of this delay.

89. The Organization agreed fully with the recommendation. It added that an internal TC review is currently actively engaged in the update of certain TCE project cycle related procedures including those for operational clearance and operational closure. In addition, TC is working closely with the CSF to ensure implementation of the recommendations.

90. Following restructuring within the Department, as of January 2010, TCSR is now in charge of operational support issues, including oversight of operations. In this capacity, it has launched a series of missions to the ROs, in cooperation with other divisions and units in TC Department with the aim of identifying, assessing and solving operational delays and problems, including those related to project closures. We were also informed that, TC Department's Operations Support and Resource Mobilization Missions to ROs have been amplified in scope to include projects from all sources of funding, both technical cooperation and emergency, and have been designed to review in depth the current situation of activities in the field with a view to promoting more effective and efficient implementation and monitoring throughout the project cycle, including terminal reporting, project closure and financial management; and a new monitoring tool has been designed within FPMIS in support of these activities.

Support Costs to Field Programme (Project Servicing Costs)

91. We audited the support cost expenditures and recoveries. The audit was aimed at determining if the support cost policies as applied provided the results as intended by the Governing Bodies and if the support cost expenditures and recoveries are presented fairly in the financial statements.

92. In the implementation of projects funded thru EB funds or voluntary contributions, the Organization charges some costs that it incurs in carrying out the activities pertinent to said projects. These support costs are categorized as Technical Support Services (TSS) and Administrative and Operational Support (AOS). While TSS are mostly costs directly traceable to the project, the AOS are indirect variable costs which are spread over administrative and operational posts, many of which do not provide full time support in project implementation. Since AOS are not readily identifiable with the projects, these are reimbursed generally through a percentage charge on project delivery known as Project Servicing Cost (PSC).

93. Several factors and cost components are considered in the computation of the TSS and AOS services and these are then divided by the total field project delivery to come up with the TSS and AOS rates for the biennium.

94. We noted, however, that in the case of AOS indirect project support costs, the methodology excludes the following elements of fixed indirect costs:

a) all costs related to the ADG Offices excluding the Management Support Units (MSUs);
b) all fixed overhead costs related to the operation and maintenance of the information technology infrastructure by CIO;
c) all costs of the operation of the financial system except the CSF units directly responsible for UNDP and Trust Fund accounting which are treated as indirect project support costs;
d) all costs of administering the central personnel function by CSH;

e) costs of space, security, communications (except those charged directly to projects), messenger service, central records and procurement for Regular Programme activities administered by CSA - although CSAP costs related to project procurement are treated as indirect project support costs;
f) costs of regular budget preparation, control and evaluation by OSP, although costs of project budgetary control and evaluation are treated as indirect project support costs or, in the case of evaluation missions, as direct project costs;
g) costs of legal services provided by LEG, excluding technical services to projects which are treated as direct project costs (see TSS below); and
h) costs of Internal Audit and External Audit excluding direct services provided to projects. (FC 94/4 (c), para. 18, JIU/REP/2002/3, para. 29-30)

95. While consistent with the current approved support cost policy, the exclusion of these fixed indirect costs in the methodology used to calculate support costs to field programmes means full absorption of such costs by the RP funds and a definite subsidy to the EB funded programmes and projects. It is difficult to see how such elements should not be considered for recovery considering the level of donor funded programmes and projects had already exceeded half of the total expenditures of the Organization from all sources.

96. The exclusion of these indirect fixed costs has to be reconsidered because, notwithstanding the exclusion of indirect fixed costs in the support cost policy, the Organization is already recovering certain indirect fixed costs such as costs of office space at headquarters occupied by project staff and contributions toward the ASMC liability. Several others, however, are currently directly charged by some Organizations but not by FAO, such as office space at regional, subregional and country level and central information technology infrastructure, and portions of security costs (FC 128/13 para. 13-14). This has not been readily embraced within the support cost policy such that guidelines could have been already put in place and the appropriate training of staff conducted in the recovery of indirect fixed cost. We note that the changes already made by the Organization to recover some of these costs such as office space may be questioned in the absence of a clear updated policy on support costs.

97. We noted, however, that the High Level Committee on Management (HLCM) Finance and Budget Network (FBN) Working Group on Support Costs had completed an inter-agency study which considered as among the recommendations the recovery of four types of administrative and operational support costs, one of which is ‘certain fixed indirect costs’. The Administration had already sought the guidance of the Finance Committee (FC), that once the HLCM-FBN has had an opportunity to finalize its recommendations, FAO will undertake an internal review to determine the most appropriate approach of implementation including through the development of corporate guidelines for the preparation of budgets and cost recovery for activities funded by voluntary contributions (FC 128/13 para. 19).

98. The current policy on PSC rate sets the ceiling at 13 per cent of programme or project delivery. The ceiling rate is another aspect of the support cost policy that makes it difficult for the Organization in achieving a reasonable alignment of the AOS costs (as they actually materialized) and reimbursements in cases where former is lower than the latter.

99. While the actual AOS costs are not yet available at the time of audit, it has averaged at the rate of 12 per cent of the field programme delivery from 2000-01 to 2006-07. The actual AOS cost, however, had exceeded the PSC ceiling rate of 13 per cent in both 2004-05 and 2006-07 when they reached 14.1 per cent and 13.7 per cent respectively. Applying these percentages to the total field program expenditure for the respective bienniums results in an estimated USD 12.9 million of AOS support costs having been absorbed by RP funds instead of being reimbursed from EB funds.

100. Given the foregoing conditions that make it difficult for the Organization to realize reasonable alignment between the AOS costs (as they had actually materialized) and their reimbursements from EB programmes and projects, we highlight the consistent under recovery of these AOS costs. From 2000-2001 to 2006-2007, the AOS recovery averaged only at 7.8 per cent of the total field programme delivery compared with actual AOS costs which averaged 11.8 per cent of the same total delivery figure.

101. The TSS reimbursement rate is similarly low compared to the actual TSS costs as the average in the last decade was only at 2 per cent of the field programme delivery compared to the 8.9 per cent average actual costs from 2000-01 to 2006-07.

102. Management emphasized that there was a difference in the conceptual and legal framework for the provision of TSS foundation compared to AOS. While FAO Governing Bodies advocate for the full cost recovery of AOS costs from voluntary contributions, the provision of technical assistance to Members is mandated in the Constitution of FAO Article I 3(a). This implies in turn that the funding for such technical assistance (TSS) may legitimately come from assessed contributions, when the recovery is not possible. However, instances where recovery is possible or not have not been adequately articulated while the extent at which the Organization desires to recover the cost of TSS have not been established yet.

103. Any shortfall in the recovery of support costs to field programme and projects under the current policy can be reported and assessed considering that it may be represented by the following:

a) gap between the AOS costs as they had actually materialized (both fixed and variable) and support costs reimbursed; and
b) difference between the TSS costs as they had actually materialized and TSS reimbursed.

104. We have noted in certain reports of the Organization regarding recovery of support costs from field programmes and projects that these reports did not deal in adequate detail on the extent of reimbursements as a reflection of the current policy on support costs. In particular:

a) the biennial Programme Implementation Report practically presents only in total the difference between the actual support costs to field programme and reimbursements;
b) while approved variations from the PSC ceiling of 13 per cent are reported to the FC by project category, the actual reimbursements of AOS costs are not assessed per project category;

c) while the AOS costs are being recovered through fixed percentage, direct charge or combination of the two, the actual reimbursements are not assessed and reported by the method they were reimbursed; and

d) as previously mentioned, support costs to field programmes and projects are fully budgeted in the PWB. These are budgeted either as income or expenditure. The budgeted support cost income represents the expected level of reimbursements and is distributed to those who carry out the administration and operation support. While the actual income of the Organization is reported in Financial Statement IV and any issue arising from the level of actual reimbursements is reported to the FC in the Annual Report on Budgetary Performance and Chapter Transfers, the actual reimbursements of support cost to field programmes against the corresponding budget are not readily discernible as indicator of reimbursement efforts.

105. Further, the support costs to field programmes and projects that should have been reimbursed from donor funded programmes and projects, but absorbed by the RP funds, were not evident in the financial statements of the Organization. These unrecovered support costs were merely presented as part of the total AOS costs and TSS of the Organization. An appropriate disclosure of the unrecovered AOS costs and TSS from the donor funded programmes and projects, for example, could have readily informed the readers of the financial statements that the delivery of field programmes funded by EB funds actually cost more.

106. We recommend that the Organization**:**

a. in accordance with the principle of reasonable alignment of support costs to field programmes and projects as they had actually materialized and recoveries from donor funded projects, work on the immediate expansion of the policy on support cost reimbursements to include recovery of any fixed indirect costs as far as already acceptable to donors and can be made acceptable to them and provide for the appropriate guidelines and training required.

b. in accordance with the principle of transparency and in order to accurately establish the reasonable level of support cost reimbursements, consider reporting and assessing the level of reimbursements of support costs from EB funded projects to show the following:

b.1 unrecovered fixed indirect support costs;
b.2. unrecovered support costs by category of programmes or projects;
b.3. unrecovered support costs represented by the difference between the approved TSS and PSC rates and actual reimbursements; and
b.4. unrecovered support costs represented by the difference between the support cost income budgeted and the actual reimbursements by manner of recovery (fixed-percentage charge, direct charge to programme or project or combination of the two).

c) in order to present fairly the support costs actually incurred under the RP funds, consider the disclosure in the financial statements of the unrecovered support costs from donor funded projects and absorbed by the RP funds and how these were calculated.

d) in keeping with the principle of reasonable alignment of support costs to field programmes and projects as they had actually materialized and recoveries from donor funded projects, and in order to accurately establish the reasonable level of TSS cost recovery:

d.1. consider articulating the instances where recovery is possible or not; and

d.2. establish the extent at which the Organization desires to recover the cost of TSS**.**

107. Management commented that while the principle of reasonable alignment of support costs to field programme is desirable, the same may have to be implemented incrementally considering the under-recovery of indirect variable costs and the ceiling on what donors are prepared to pay. On reporting and assessing the level of reimbursement of support cost from EB funded projects, it would consider the same taking into consideration the cost benefit particularly in the case of an incremental application, and considering also the reporting mechanisms already provided to the Governing Bodies on support cost recoveries. The Organization also noted our recommendation on the disclosure in the financial statements of the unrecovered support costs and would consider it taking into account the reporting already being provided to the Governing Bodies and considering the timing of the cost measurement study upon which such comparison depends.

Property Management - Custody and accountability over non-expendable property

108. We noted that property management could be improved. In particular, issuances of non-expendable items to staff members had not been documented as required by Section 503.2.12 of the FAO Administrative Manual. While the Custody of Property form is required to be filled up by the staff member when a property item is issued, the practice is to list all property items in the name of the particular Office/Division.

109. The determination of accountability is critical as Section 503.1.423 of the same manual states that a staff member is financially liable for any loss or damage to a property unless he/she is relieved of this liability by the Organization. When loss or damage occurs, the Organization may withhold the appropriate sum from payments due to a staff member.

110. In our review of the FAO Assets by Owner Report (Inventory Report) as at 31 December 2008, it was revealed that 89 items consisting of computer units, printer and photocopying machines could no longer be found and their status remained undetermined. The reason(s) why these could no longer be found was not known. Consequently, the persons who should have been accountable therefore could not be identified as there are no documents that could have provided such information.

111. We also noted that in taking out valuable property items from the Organization's premises, a staff member was not required to secure gate passes from the Security Unit.

112. We acknowledge Management's general agreement with the overall observation about better control over non-expendable items. Management added that the modality of its implementation shall also depend on the changes in asset management processes, which is presently in the midst of change and reform because of (a) the offshoring of the assets function to Budapest and (b) the business process change due to the IPSAS project. Thus the Manual Section governing this area is still under revision.

113. We recommend that issuances of property to any staff member be documented by a Custody of Property Form and that the listing of properties in the name of the division be used only for common equipment such as printers, and photocopiers or divisional (shared) laptops. We further recommend that staff members be required to secure gate passes before a property item is taken out of office premises.

Non-expendable property and Expendable property

114. Policies and procedures pertaining to the recognition of non expendable property (NEP) need re-examination as these did not ensure uniform valuation of the NEP. This deficiency ran counter to the objectives in the adoption of the United Nations System Accounting Standards (UNSAS), which embrace the consistent and transparent treatment and disclosure of financial transaction.

115. For the current biennium, purchases of supplies, equipment, furniture and motor vehicles amounting to USD 398.702 million (USD 71.463 million for General and Related Funds and USD 327.239 million for Trust and UNDP Funds) or 18.21 per cent of the total expenditures was disclosed as purchases of equipment in Note 10 (titled as Expenditures) to the financial statements. On the other hand, in Note 31 (titled as Other Disclosures – Equipment, Furniture and Vehicle), the amount of USD 129.225 million was shown as the balance of non-expendable equipment, furniture and vehicles as at the end of the financial period.

116. Our review of the Notes to financial statements readily revealed that the valuation method used in recognizing non-expendable property as purchases and as inventory was inconsistent. Purchases of non-expendable property were recorded in the general ledger (GL) and recognized and disclosed in Note 10 at historical costs and therefore included additional charges such as freight and insurance. On the other hand, the amounts disclosed in Note 31 as the historical costs of equipment, furniture and vehicles and supported by the Annual Additions Report generated from the Oracle Fixed Asset (OFA) Module pertained to purchase prices excluding the additional charges.

117. The Organization confirmed that the latter basis of valuation of equipment, furniture and vehicles had been consistently applied in prior biennia and that the definition of the threshold for non-expendable items as reflected in the administrative manual for property accountability (Section 503.1.3) specifically excludes "additional charges such as freight and insurance".

118. Section 50 of the UNSAS provides that at the end of the financial period the inventory value at the beginning and end of the financial period of non-expendable equipment, furniture and motor vehicles and the method of valuation (cost or valuation) should be clearly stated in a note to the financial statements. Where possible and to the extent required by the financial policies of the Organization, additions and disposals made

during the financial period should also be disclosed. Historical costs or acquisition costs, as defined in the Accounting Reference Manual and IPSAS, include the purchase price, freight and handling charges and other incidental expenses relative to the purchase.

119. Further, Note 31 disclosed the inventory at the end of each biennium but did not provide clear information on whether the ending balance of the previous biennium is the beginning balance of the current biennium as required under the UNSAS. We also noted that there were no disclosures on total asset additions and deletions. Our examinations also revealed that the inventory balance was potentially misstated although due to the limitations of the asset recording and valuation system, the amount of the misstatement could not be determined.

120. As earlier discussed, purchases of fixed assets were recorded in the OFA excluding incidental costs while these were recorded in the GL using historical costs. The current system did not permit us to establish the correct valuation of the inventory with accuracy as it would entail a review of individual transaction including those in the beginning balances.

121. Our review of the sample purchase orders revealed that USD 0.92 million or 30 per cent of the amount sampled was not recorded in OFA and accordingly were not disclosed in the Notes. Additional inquiry revealed that the discrepancy was due to the delay in the recording of acquisitions by the Asset Unit in view of the tedious manual entry to OFA and the volume.

122. We recommend that the Organization revisit its policies and procedures in the recognition of non-expendable property and that the valuation method used in recognizing non-expendable property as purchases and as inventory are consistent.

123. To facilitate recording in OFA and to minimize account misclassification, we reiterate our previous recommendations that the Organization consider the (a) interfacing of the Oracle Purchasing (OP) and OFA with the Category Code of the item as the common link; and (b) electronic transmission of data on local purchases made by field offices with internet connection in MS Excel for uploading to OFA. We also suggested that the Organization consider the implementation of the receipts functionality of the OP, which may later be linked to OFA for the computation of depreciation expense, in preparation for IPSAS implementation. We, likewise, encouraged the Organization to present information relative to asset additions and deletions during the financial period.

124. The Organization confirmed that as part of the wider review of changes in processes to address IPSAS compliance requirements it will be reviewing and implementing updated/new processes for the identification of and the accounting for property, plant and equipment and the required financial statement presentation and disclosures.

Year End Asset Reports

125. The results of our audit revealed that the mandated timing of the submission of the Year End Asset Report (YEAR) by the Field Offices to the Headquarters, the inability of some field offices to return to the HQ the YEAR with their corrections thereon, and the

non-reconciliation of inventory records within the offices in the HQ did not permit the timely updating of the FAO records to reflect the correct information on the Organization's property and equipment.

126. We noted that the pertinent Manual Section requires the Offices outside HQ to submit YEAR by the end of April while the financial statements where Note 31 is disclosed is required to be submitted under the Financial Regulations not later than 31 March of the year following the end of the biennium. As of the time of submission of the financial statements, the inventory disclosed therein may not be correct and adequate as it did not have available information on the existence and condition of the assets that are contained in the YEAR.

127. We, likewise, confirmed that for the 2009 year-end asset returns, inventories in the HQ were not checked as to existence and condition and were not reconciled with inventory records because of on-going physical relocation of staff and their assigned property due to HQ restructuring, and closure of projects and transfer of assets during the period when the asset return is due to be prepared.

128. We also learned that responsibility for updating inventory records for field location was offshored to Shared Services Centre, Budapest starting 2010 and that reports for CY 2009 from country offices were not yet complete, hence, information on the existence and condition of the assets cannot be verified and reconciled with the inventory records or with the OFA. In the absence of duly verified and reconciled YEAR, vital information pertaining to asset deletions due to loss, write-off as well as asset condition, and asset additions such as donation, among others, will not update the OFA which generates the report that supports the amount disclosed in Note 31 of the Notes to the financial statements. Thus, the amount of non-expendable property disclosed in Note 31 may not be correct as to existence and valuation.

129. The Organization commented that the updating of information relative to asset additions, deletions, write-offs and donations is a continuous process completed during the year, which is independent of updates arising from the year-end asset verification. We want to point out that although updating is a continuous process, appropriate cut-off dates need to be established for the purpose of reflecting the correct information on the financial statements.

130. We recognize that the Organization is revising its asset management policies and procedures within IPSAS and recommend that the Organization ensure that the submission of YEAR by the Offices outside Headquarters as to the timeline of submission, the monitoring of their submission and the immediate verification and reconciliation of property records in the Organization, is included in the new policy.

131. The Organization recognized that significant changes and improvements of the existing processes would be required to support the accounting for property, plant and equipment in order to meet IPSAS requirements and the Organization would be performing a detailed review of these processes in the context of that project.

Field Advances – Advances to Staff Members for Tax Payments

132. We sampled 56 advances for tax payments and noted that 18 or 32 per cent were settled beyond the prescriptive period and 9 or 16 per cent remained unsettled as at 30 April 2010. Also tax advances for 48 staff members amounting to USD 0.462 million and USD 0.023 million and pertaining to taxable years 2008 and 2007, respectively, and were all considered overdue as at 31 December 2009.

133. Management further commented that for tax years prior to 2009 where tax advances exceeded the liability, the staff member was entitled to elect to carry forward the excess to future tax periods as provided for in the US tax rules. As part of the ongoing efforts of the Organization to improve the follow up of advances, all staff members who have received tax advances to pay estimated taxes must now clear those advances by submission of their tax return by the September month following the tax year to which the advance relates. Any advances not so cleared by the September due date will now be recovered from the salary of the following month. Management further commented that it is currently liaising with its Washington office in creating a system that would ensure the timely recovery of the overdue advances and the most effective and efficient way of receiving the feedback.

134. We note that the previous option to apply the excess tax advances to future tax years combined with delays in, and the non-submission of tax returns and their supporting documents hampered the determination of whether the outstanding tax advances have been settled and refunds or recoveries are due at the end of the prescriptive period of settlement.

135. We were informed of the improvements made in the policies related to the recovery of tax advances. However, we still recommend that the Organization through its Liaison Office in Washington require the strict enforcement of the submission of the annual tax returns within the deadline set in the Administrative Circular AC2010/08 so that prepayments are promptly cleared and excess advances refunded immediately by the staff members.

Field Advances – Advances to Consultants

136. Field advances to consultants represent advances that were disbursed by decentralized offices for expenditures related to project activities for which no local representation is available to make the disbursements. These are called Operational Cash Accounts (OCA). The purpose of an OCA is to support temporary operational activities in locations where there are no banking facilities available, where opening of a bank account is not feasible, or where direct payments from an FAO office are not possible. Under DGP046, these advances must be cleared by the submission of expense reports and any monies not cleared are recoverable from the consultants.

137. A sampling of 55 outstanding advances amounting to USD 598,000 revealed a number of issues. It should be noted that 15 (USD 167,000) out of the 55 subject field advances were outstanding for more than 90 days. Also, 16 advances were cleared in the first quarter of 2010 resulting in the erroneous recognition of expenditures of USD 431,000 in the same year. As DGP046 further requires that OCAs arrangement should last no longer than three months, the advances granted three months prior to end of the

year should have been expended within the year and recorded as expenses of the 2008-2009 biennium instead.

138. Additionally, it must be pointed out that DGP046 also provides that (a) each staff member, consultant or National Project Coordinator can have only one OCA outstanding at any one time, and (b) OCAs must not exceed USD 10,000 or the local currency equivalent.

139. In our review, we observed that there were six consultants with multiple outstanding advances as at 31 December 2009. Two of them held seven and eight advances each aggregating USD 313,000. Likewise, in 16 of the 55 outstanding advances, the USD 10,000 limitation was exceeded.

140. Management observed that the Organization generally ensures that field advances are cleared on a timely basis and that the majority of the overdue advances identified related to one country only. It expected that all advances at the year-end would be cleared in subsequent periods and noted that the clearance of advances in the first quarter did not "necessarily indicate that the expenditure had been incurred at the year end. It further explained that the single country where the majority of the overdue field advances had originated referred to a situation with particular operational difficulties, including a lack of banking system in some areas of the country, and lack of adequate infrastructure to transport documentation from remote locations to FAO office

141. We wish to point out that based on our audit, expenses amounting to USD 431,000 were indeed expenditures properly chargeable against the biennium and not to year 2010.

142. We were informed that the majority of the overdue advances have been paid to consultants operating in one country and appreciate the Headquarters' effort to work with the FAO Representation (FAOR) and the Technical Cooperation Department to address the situation.

143. We emphasize the importance of an intensive monitoring effort and the importance of ensuring the timely settlement of advances especially those remaining uncleared beyond the prescriptive period and that the grant of advances for OCAs be limited to the restrictions of DGP064 so as not to unduly burden the consultants and allow for the immediate settlement of the said advances.

Field Advances – Others (Payroll Writeback)

144. We observed that outstanding prepayments which are due for recovery also include 101 prepayment invoices amounting to USD 226,000 classified as payroll writeback. These invoices represented receivables from staff members due to their negative net pay.

145. According to management, reimbursements of 45 per cent of the total balance amounting to USD 102 thousand was made in February 2010 and early March 2010 and follow up action is continuously being undertaken in order to obtain the reimbursements of the entire balance.

146. We recognize the steps taken by Management in recovering these advances and recommend that sustained efforts be made to collect the remaining payroll writebacks.

Technical Cooperation Programme Deferred Income

147. The Technical Cooperation Programme (TCP) is a Regular Programme activity funded through assessed contributions from Member Nations contributions. TCP appropriations are available over two biennia and any excess of the appropriation over expenditures for projects in the first biennium is recorded as deferred revenue and is carried forward to be fully utilized in the following biennium (Accounting Reference Manual). FAO Financial Regulation (FR) 4.3, however, requires that all appropriations unutilized at the close of the financial period following that during which the funds were voted or transferred, including that of TCP, shall be cancelled.

148. Our review of transactions disclosed that at the end of Biennium 2008-2009, an unutilized budget of USD 5 million was absorbed through the “return flow process” as disclosed in the Programme and Finance Committee Joint Meeting Report JM 2010.1/2. There were 11 projects, subject of the return flow, that were originally approved against the 2008-09 appropriations but were instead charged against the 2006-07 appropriation so that the expenditures against the TCP appropriation for 2006-07 would reach 100 per cent of the net appropriations of USD 95.70 million.

149. In its comments, the Organization explained that FR 4.3 restricts the period during which obligations may be incurred against the TCP appropriation to two financial periods (i.e. four calendar years). The return flow process, it said, is fully consistent with the FR since the expenditures which are reclassified as part of this exercise have been incurred in accordance with the periods set out in FR 4.3 when obligations may be charged against an appropriation. The return flow exercise, they contended, only reflects a reclassification of the appropriation period against which the expenditures have been originally charged, fully respecting the restrictions of FR 4.3.

150. A reading of FR 4.3 will readily reveal the intent to cancel unutilized appropriations for programs/projects financed for that appropriation period. The records revealed that the 11 projects referred to above were funded under the 2008-2009 appropriations. While the obligations were indeed incurred during the latter financial period, these pertain to projects that should be financed under the 2008-2009 appropriations and not by the 2006-2007 appropriations. The amount of USD 5.013 million should have been cancelled.

151. We recommend that the Organization implement TCP projects within the terms of the existing FR 4.3, specifically the cancellation of unutilized appropriation at the close of the financial period for which the appropriation was voted for to ensure proper programming and implementation of project activities within their approved budgets and appropriation for the year/biennium.

Plan Assets

152. As at 31 December 2007, the Organization changed its accounting policy for after service benefits as part of an overall effort to move FAO toward full adoption of IPSAS. The expense rates and liabilities are determined by actuarial valuation.

153. In its Financial Statements the Organization has Long Term Investments (at Fair market value) of USD 294.71 million and advances on Separation Payment Schemes (SPS) of USD 10.149 million as of 31 December 2009. These amounts or part thereof could have been earmarked as a separate fund or trust for the sole benefit of plan participants and appropriately constituted as Plan Assets within the purview of IPSAS 25.

154. IPSAS 25 defines Plan Assets as comprising of (a) assets held by a long-term employee benefit fund and (b) qualifying insurance policies. Assets held by a long-term employee benefit fund are those assets (other than non-transferable financial instruments issued by the reporting entity) that:

(a) are held by an entity (a fund) that is legally separate from the reporting entity and exists solely to pay or fund employee benefits; and

(b) are available to be used only to pay or fund employee benefits, are not available to the reporting entity's own creditors (even in bankruptcy), and cannot be returned to the reporting entity, unless either (i) the remaining assets of the fund are sufficient to meet all the related employee benefit obligations of the plan or the reporting entity; or (ii) the assets are returned to the reporting entity to reimburse it for employee benefits already paid.

155. While the intent of the Organization to consider the long-term investments and advance payments for the SPS, is reflected in FC reports, disclosures in the financial statements and other records, no steps have yet been taken to constitute them as Plan Assets within the context of IPSAS 25.

156. Had these assets been constituted as Plan Assets, IPSAS provisions would allow the plan assets to be offset against the related staff liability, reducing the reported balance of the staff liability reported on the face of the financial statements. These provisions would also allow the return on Plan assets to be recognised and to reduce the annual expenses represented by expected return of US D 0.661 million as reported by the actuary in 2009. In addition, the establishment of a separate fund or trust to hold the Plan Assets would provide further protection over such assets to ensure that they can be used only for the benefit of the employees in meeting the Organization's staff-related obligations.

157. We recommend that the Organization consider placing the earmarked long term investment and advance payments for the SPS in a separate trust fund to properly recognize them as Plan Assets as part of the effort towards full adoption of IPSAS 25.

158. The Organization noted that it would review the recommendation to place the earmarked assets in a separate trust fund within the context of IPSAS implementation.

Procurement - Liquidated damages on late deliveries

159. We urge the Budget Holder (BH) to be more circumspect in the performance of their duties. Based on the prevailing practice in the Organization, the BHs review the Purchase Order (PO) and the pertinent deliveries made and recommend the payments. As such, they are in the best position to ascertain compliance by the suppliers of the terms of

the PO such as conformity with specifications of the delivered items and timeliness of the deliveries.

160. The results of the audit would show the delays in the deliveries of sampled items ranging from two to fifteen weeks. In the payments subsequently made, we found no evidence that liquidated damages were imposed against the concerned suppliers although the imposition of such penalty was contained in the PO. In essence therefore, it appeared that the BHs were unable to monitor the deliveries, note the delays and consequently recommend the imposition of liquidated damages before the payments were made. Management informed us that in one of the delayed delivery example taken by the Auditor, the Organization took action with the supplier (additional discount) which resulted in savings which were three fold the amount envisaged under the standard application of penalties while maintaining the good relationship with the supplier. In addition, Management noted that there were other issues on some of the delayed deliveries (such as additional requests by the Organization) after the PO was issued which clouded the strict cut-off date for delivery.

161. However, Management agreed with our recommendation that BHs must monitor the deliveries and recommend the imposition of penalties. However, it noted that in the absence of a record of the receipt of goods in the financial system, it is not presently possible to systematically identify POs with late deliveries and accrue such penalties in the books. Additionally, it mentioned that the accrual of penalties will be reviewed in the context of the implementation of the receiving process as part of the IPSAS project.

162. We recommend that the monitoring of deliveries be strictly performed by the BHs. The recommendation to impose penalties, if any, should be made by him/her already and subsequently deducted from the payment.

Travel – Ticket Cancellations

163. We analyzed the causes for travel cancellations which were culled from the pertinent Travel Authorizations in the travel system ATLAS and from the replies sent by the Travel Unit. Causes of the cancellations attributable to the traveller such as no-show, unplanned trip, self-purchased tickets and changed itinerary accounted for 66 per cent; lapses of the Division concerned such as booking a ticket for a traveller without a visa, postponed mission, unauthorized travel or travel without available local funds represented 16 per cent; errors committed by the Processor 7 per cent; and unforeseen events, such as sickness and weather, 11 per cent. It can then be deduced that 89 per cent of the causes were due to lapses committed by either the traveller or the processor which may be preventable and only 11 per cent pertained to unforeseen events.

164. Inspite of the causes being connected with the traveller or the Division, all charges including the full costs of the issued or rerouted tickets were borne by the Organization. We believe that the practice was not in conformity with Staff Rules 302.7.335, which provides that when deviations are made from approved travel plans, the Organization's liability shall be limited to the maximum expense and travel time which would have arisen had travel been carried out by the approved route, mode and standard of accommodation. Further, FAO Administrative Manual Section 401.3.12 requires that Staff members must pay directly to the Organization's travel agent or must reimburse to the Organization any costs in excess of the Organization's liabilities.

165. Management commented that the application of this policy is used in the context of the change in itinerary, the mode of transport and the class of travel used and does not include other causes attributable to the travelling staff member.

166. We believe though that the causes of the cancellation of tickets were attributable to the traveller, all charges including costs of ticket cancellations should be charged to him/her. In this context, we recommend that the Organization set a policy that will hold the traveller accountable for the cost of tickets, surcharges and fees in cases where cancellations are caused by him without justifiable reasons. The Organization noted that it will review the impact of such a policy within the context of the staff rules. Simultaneously a communication strategy will be undertaken to sensitize budget holders and approvers of cancellations charges to the cost of cancellation and the need to determine upfront the validity of these charges.

Special Fund for Emergency and Rehabilitation Activities

167. SFERA seeks to improve FAO's capacity to respond to emergencies. Its three components are: (a) a revolving fund to support FAO's involvement in Needs Assessment, programme development and early establishment of Early Coordination Units; (b) a working capital component to advance funds to initiate project and activities rapidly before donor funds on agreed projects are received, with the funds then being transferred back to SFERA upon receipt; and (c) a programme component to support work on specific large-scale emergency programmes.

168. The Accounting Reference Manual provides that funds may be applied either (a) as an advance in the expectation of recovery from donor contributions directly to the activities/project concerned (Advances) or (b) as funding for activities for which direct donor contributions are not sought/expected and will not be reimbursed (Applications).

169. We reviewed advances and applications of the SFERA for the period January 2008 to December 2009 and noted that there were no definitive guidelines on (a) the amount of the advances that may taken out of SFERA to initially fund a specific project or undertaking and (b) the period of time within which the advances will be returned to the fund.

170. We observed that the amounts of advances ranged from USD 100,000 to USD 3.5 million per project. In one project, the advance of USD 3.5 million made in February 2009 represented 77 per cent of the original approved budget of USD 4.5 million, despite approval of an early funding of USD 4.5 million a month earlier from the Office of UN Resident and Humanitarian Co-ordinator for the Sudan. In another project, an advance of USD 100,000 constituted 88 per cent of the original approved budget of USD 112,714.

171. The Organization highlighted that the proportion of a project's budget which an advance represents has limited significance and considered of more importance is the legally binding contract with the donor to pay the entire budget amount.

172. Our analysis also showed that refunds of advances were made from six to fourteen months from the date of grant and that the total advances made in 2008 of USD 6.77 million that remained outstanding for more than the average time of three months had

brought down the 2008 fund balance of USD 13.89 million from the 2007 balance of USD 21.35 million.

173. The Organization informed us that the average time outstanding for all advances is close to three months. It added that while the rules for the governance of the SFERA did not specify a maximum period an advance may be outstanding, regular monthly follow up of outstanding amounts is carried out by TCE.

174. While we take note of management's justification, we still believe that guidelines with regard to the amount of advance funding that may be allowed and the specific period within which the advance will be recouped will contribute to the stability, rational and systematic allocation of SFERA funds to projects that need immediate implementation.

175. Along this line, we recommend that the Organization pursue the formulation of guidelines for the SFERA that will specify the maximum amount of the advances that may be granted to a specific project and the definite period within which the said advance will be recovered**.**

PART III

AUDIT OF DECENTRALIZED OFFICES

Budgetary Controls – Regular Programme (Regional Office for Africa)

176. We assessed the budgetary controls prevailing in the decentralized offices and observed that there was a pressing need to exercise adequate controls over allotments and expenditures. The existence of over-expenditures in some programmes reflected the need for greater attention by some BH to limit their expenditures within the budget. In 2009, the Regional Office for Africa (RAF) incurred expenditures in excess of allotment amounting to USD 170,000. Similarly, it incurred over expenditures exceeding USD 20,000 in each of the two chapters (total amount was USD 1.3 million) and exceeding USD 100,000 in each of the four programmes and for which no approval of the Director, OSP was sought. In certain instances, the excess over allotments (for programmes) ranged from 34 per cent to 632 per cent. The excess was exacerbated by the fact that shifts between programmes, although allowable under certain conditions, would no longer be possible as the allotment balances of other programme are negligible to accommodate the excesses. It is worthy to mention that there were no evidences that would substantiate any prior approval on these over-expenditures.

177. We noted that the Periodic Budget Performance Reports (PBR) at RAF were regularly submitted to OSP with explanations on planned activities, explanations on deficits and resources generated from vacant posts along with forecasts of expenditures entered in the Budget Maintenance Module (e-BMM). However, there were no specified requests showing proposed amounts for shifts between programmes within a chapter or between chapters. While we recognized the desire and effort of the RO to fully utilize the available resources for other programmes needing additional resources, the fungibility rules requirement on prior approval for shifting allotments exceeding certain amount must be complied with.

178. Verification from Programme Planning, Implementation Reporting and Evaluation Support System (PIRES) PBR node, where the review and authorization of resources shifts by OSP may be viewed, however, revealed that the node did not reflect any comment on the submitted PBRs by RAF for the biennium 2008-2009.

179. Inquiry from the Programme Planning and Budget Unit (PPBU) at RAF on the over-expenditures disclosed that extra resources generated in five programmes due to nine post vacancies were used in programmes with deficits in allotments, and PPBU explained there was no explicit contention of this specific shift of resources. It was also mentioned that Oracle financials did not prevent them from incurring commitments and expenditures beyond the allowed budget flexibility. Furthermore, Management noted that it had begun to address the issue of vacant positions through creation of a task force dedicated to monitor regularly the status of this RAF's vacancies

180. While we took note of the explanations, we maintain that prior approval of resource shifts by RAF as required in the budget fungibility rules should be obtained on forecasted expenditures. In this context, it should be noted that the Director-General is enabled, under Financial Regulation 4.5 (b) to effect transfers from one budgetary chapter to another upon approval by the Finance Committee and/or the Council.

181. We recommend that the RAF enforce more strictly the requirement to secure prior approval from OSP before incurring commitments and expenditures requiring shifts of allotments exceeding USD 100,000 at programme level and USD 20,000 each at chapter and allottee levels. RAF's request for shift, which may be included in the PBR, needs to state specifically the allotted amounts to be shifted, the source of allotment for transfer between programmes or chapters and the reasons or justifications for the transfer. We also encourage RAF to work consistently within the limit of the institutional allotment provided in accordance with the PWB.

Budgetary Controls – Projects
(Regional Office for Africa)

182. Based on our audit, we believe that budgetary controls at the Regional Office for Africa (RAF) could be strengthened for extrabudgetary programmes. The BHs maintain operational control over the project including the budget. As such, he is being guided by the project budgets, which define the project inputs and deliverables, the Field Programe Management Information System (FPMIS) and the Oracle Data Warehouse (ODW).

183. The FPMIS which is available in FAO offices to provide corporate information on FAO Field Programme, generates automated messages advising the BH that commitments and expenditures cannot exceed the approved budget or cash available (net of interest) to the project. The FPMIS has also built-in capacities to send emails to the BH/FAO representatives concerned, reminding them of some housekeeping actions for issues affecting financial and operational management of the projects.

184. For Trust Fund projects, the BH will have to monitor the cash balance in the ODW to the best of his/her ability in order to avoid any over-commitment/over-expenditure and alert Finance Division (CSF) on the need to obtain additional

contributions from the donors as per approved schedule of Calls for Funds. A tool is also available from the Frequently Asked Questions (FAQs) in the FPMIS.

185. These tools are available to the BHs in general, however it was noted that in the case of RAF conditions to enable optimal use of these facilities need to be strengthened. It was noted that RAF incurred negative cash balances amounting to USD 641,189 in four projects due to excess of expenditures over the cash received. The excess ranged from 2.9 per cent to 122.6 per cent and of these negative amounts, USD 600,432 (94%) referred to one project where there had been a delay in requesting the call for funds from the donor.

186. We are appreciative of management's commitment to improve the controls necessary for the BHs to work within the approved budgets and cash received from donors. Coordination would likewise be strengthened with the Headquarters to facilitate the request for Call for Funds and submission of budget revisions needing donor's consent and approval to prevent incurrence of negative balances for TF projects.

187. We recommended and RAF agreed that the Budget Holders endeavour to work within the approved project budget for TCP, and in the case of TF project within the cash received from donor. To ensure that funds are available for the project before incurring commitments and expenditures, the BH should consider employing worksheet of actual commitments and expenditures outside of the existing systems to keep track of project cash or fund balance until system embedded controls to prevent over-expenditure are put in place. In the event that the cash balance is low and there is a need to obtain additional cash from the donor and as required in the Project Agreement, the BH needs to promptly request from the Finance Division – Project Accounting (CSFE) the need for the Call for Funds and submit budget revision needing donor's consent/approval to prevent incurrence of negative cash balance for TF projects.

Non-Expendable Properties

188. We believe that an improvement in the practices involving Non-Expendable Properties (NEP) may have to be carried out in the field offices to enhance reporting and accountability.

189. In three regional offices as well as two FAO representations, there were a number of instances when acquisitions of expendable items were booked up as non-expendable procurements and purchases of NEPs were recorded as expendable items which signified deficiency in the review of accounting transactions. Further, we observed several discrepancies between the YEAR as prepared by HQ and the records maintained by field offices such as ADM 41 (Report of Equipment Locally Purchased from Imprest Account) and ADM 83 (Report of Loss, Damage or Unserviceability of Property). The need to reconcile these records and reports became imperative as instances of NEPs being absent in the YEAR but present in ADM 41 were noted. Conversely, items were included in the YEAR but not found in ADM 41. Additionally, some items were already disposed of in the field offices but still remained recorded in the YEAR.

190. Furthermore, there were instances when ADM 41 and ADM 83 were not prepared and submitted by the field offices resulting in the difficulty in updating the centralized inventory records and performing reconciliation of NEP records between the

Headquarters and field offices. This would adversely affect the correctness and completeness of the disclosures in the Notes to Financial Statements.

191. Not to be left out is the issue of accountability. The same needs to be given due consideration as it was disclosed that properties such as laptops, camera and other movable and attractive items being used by individual staff members were not receipted or acknowledged by them through a Custody of Property Form required under Section 503.2.12 of the FAO Administrative Manual. The absence of such receipt did not establish the proper accountability over such equipment in a way that responsibility can be determined immediately in case of loss through negligence.

192. We recommend the (i) intensified review of accounting transactions; (ii) periodic and up-to-date reconciliation of the inventory records between the decentralized offices and the headquarters; and (iii) preparation and timely submission of ADM 41 and ADM 83**.**

Consultancy Contracts' Terms of Reference
(Regional Office for Africa/Regional Office for Latin America and the Caribbean)

193. FAO has several guidelines governing consultancy contracts. For one, Sections 319.1.3 and 319.8.11of FAO Administrative Manual state that the task or services to be performed or provided by the subscriber are defined in the Agreement, including deadlines for delivery of specific outputs (e.g. production of a technical report, a translation, graphics, media material, delivery of a lecture, etc.). Payment is made when the work has been completed and judged satisfactory by the designated FAO official, normally in the form of an all-inclusive lump sum, although partial payments for necessary expenses (e.g. travel and subsistence costs) or work in progress may be authorized by the responsible officer.

194. In our review of selected Personal Services Agreements (PSA) at the Regional Office for Africa (RAF), we noted instances where specific TORs that should have spelled out the deliverables of a subscriber and bind him or her towards fulfilment of his or her contractual obligation were lacking. We also noted that all corresponding Payment Request Forms were supported by a Memorandum that contained a uniform or pro-forma statement that read: "**This is to confirm that the above-mentioned person has duly completed the assignment during the following period**" (the date of period covered was indicated). The referred documents did not specify the outputs or accomplishments to be delivered as bases for recommending payment.

195. A lack of clear definition of the consultant's output could be disadvantageous to the office as performance evaluation, which is mandated under Section 319.14.4 of the same administrative manual, may not be feasible. We are also concerned that absence of TOR would impact delivery of output.

196. Moreover, our review of consultants' contracts and consultancy reports disclosed that in some instances, payments of honoraria were effected despite the absence of Quality Assessment (QA) Form. We also observed the extension of contracts without a formal evaluation of the work performed. We were informed that subsequent to our audit of RAF, the use of QA Forms is an integral part of the recruitment process throughout the Organization.

197. It is important that the work and performance of a consultant be evaluated and monitored each time a contract is renewed as well as on the completion of assignment. This will allow for the determination of whether or not the assignment had been satisfactorily completed and with the outputs being achieved as established under the TOR.

198. Likewise, the importance of performance evaluation could not be overemphasized. Such is necessary to provide information for assessing the performance of consultants/subscribers as basis for future re-engagement while also providing propriety on payments made to the consultants.

199. Inasmuch as the contract for consultancy/PSA specifically provides, as a requisite to payment, the certification of satisfactory completion of services and similarly required under the Manual afore-cited, we find said document as a desirable tool in the processing of payment and/or probable re-engagement of a particular consultant.

200. We are concerned that in the absence of the performance evaluation, the quality of the work performed might not have been appropriately considered in the extension of the consultants' services.

201. Although management stressed that the report of the consultant was cleared by the HQ/FAOR prior to payment, there was no document that would show the review and approval.

202. We recommended and management issued guidelines and a standard template including the TOR of each contract that define (i) tangible and measurable outputs of the work assignment; (ii) deadlines for delivery of outputs and details as to how the work must be delivered, and (iii) performance indicators among others. We further recommend that the TOR be linked by clear reference (i.e., Annex) as integral part to the agreement and we appreciate management's plan to integrate the same as part of the PSA.

Prepayments
(Regional Office for Africa)

203. In the course of our review of the existing practices involving the grant and settlement of travel advances to consultants at the Regional Office for Africa (RAF), we believe that greater attention by the BH on the review of final payments of honorarium is required. As revealed by our audit at RAF, 95 per cent of the total outstanding advances due for recovery (both for staff members and consultants) or USD 274,764.87 pertained to those of consultants. Of this amount, USD 205,943.15 or 75 per cent referred to advances, the recovery of which was already doubtful as the consultants had already completed their contracts and had been fully paid their honoraria. Concerns may likewise be raised in view of the fact that 85 per cent or USD 233,329.67 had been unsettled for two or more years.

204. As of April 2010, recoveries at RAF totalled USD 62,728.07 (23 per cent) but the bulk of the advances remaining outstanding accounted for 91 per cent and comprising those granted two or more years ago.

205. Section 450.5.21, Chapter IV of FAO Administrative Manual provides that Travel Expense Claims (TECs) must be submitted to the Travel Group within one month following completion of a journey while interim claims can be submitted for journeys exceeding one month. Likewise, Section 450.5.32 of the same Manual requires that recoveries are to be deducted from the staff member's salary or final honorarium of consultants if submissions of claims are delayed for 90 days after completion of journey.

206. From the preceding discussions, it can be surmised that more robust compliance with the said provisions of the Administrative Manual was required at RAF. In addition, there were indications that the BH occasionally failed to monitor the prepayments considering that they were the persons in charge with reviewing and approving the final payments of honoraria. The existence of advances outstanding for two to eight years substantiates this conclusion. As mentioned before, the probability that the Office may still collect the advances is remote considering that the consultants had already collected their full honoraria, from which the said advances should have been deducted. Locating the consultants who owed the Office would also pose a great challenge especially for those whose advances were granted six to eight years ago.

207. The Organization commented that procedures are already in place to hold the final honorarium of consultants until all advances are settled. Payment by the AP-Invoice Unit is effected only after receiving clearance from the SSC-Travel. Monitoring of outstanding advances is handled between the BH and the Receivables Unit (AFFR-Prepayments).

208. While we appreciate the effort of the Organization to prevent the accumulation and further reduce outstanding travel advances, relevant offices should coordinate with Human Resource (HR) Services and Travel Incoming-TECs, Budapest for the follow-up and collection of advances from ex-consultants who were already paid of final honoraria. We also recommend that the Organization include in the consultant's TOR the requirement on submission of TEC and the recovery of outstanding travel advance on the payment of final honorarium.

Project Management - Delays in Terminal Reporting and Closures

209. The delays in terminal reporting and closures, operational and financial of projects were observed to be prevalent in three regional as well as two country representations. In a Regional Office, the terminal reports of two projects were submitted 18 to 24 months past the Not To Exceed (NTE) date. In another Regional Office, four of ten sampled projects experienced significant delays in the submission of the reports.

210. In one particular Regional Office, the operational closure for eight projects had not been made one month to five years after their field activities were declared complete. The factors that contributed to the delays included the delayed submission of budget revisions, delayed reports and delayed property disposals.

211. In addition, we also noted the delays in financial closures of projects. Contrary to the standard requirement that financial closures must follow within 12 months after the operational closure, the same had not been made as of December 2009 even for a project that was operationally closed since February 2006. The same situation existed for projects

which had their operational closures in December 2007 (three projects) and August 2008 (one project).

212. In another Regional Office, we observed a considerable delay ranging from two to sixty-three months in the closure of projects from the supposed date of the financial closure up to 31 December 2009.

213. Delay in the submission of report also diminishes its value in providing guidance. The main purpose of the terminal report on a project is to give direction at ministerial or senior government level on the policy decisions required for the follow-up of the project, or to provide the donor with information on how the funds were utilized.

214. While we acknowledge the predicament of management as articulated in their comments to our observations, we reiterate that utmost efforts should be exerted to observe the timelines for project implementation and completion.

Recording of Expenses
(FAO Representation, Lao People's Democratic Republic)

215. In our audit of the FAO Country Office in the Lao People's Democratic Republic (FAOR Laos), we noted several instances when expenses were charged to incorrect accounts. Based on the transaction listings for 2008 and 2009 in local currency account, the Representation paid overtime expenses amounting to USD 70,703.95 although there was no budget specifically provided for the purpose. Of the total amount, USD 37,734.65 was charged to accounts 5651 – Overtime and 5652 – Casual Labor – Temporary Assistance, both under parent account 5020 – Locally Contracted Labor, while USD 32,969.30 was charged to different accounts such as Consultants, Travel, Training, Expendable Equipment and General Operating Expenses.

216. We were informed by the FAOR that no allocation was provided for in the Field Budget Authorization (FBA) in some projects, hence, overtime expenses were charged to other project funds or other accounts of the same project where budget was available. This resulted in the reduction of the budget in the accounts or project funds where overtime expenses were charged. Furthermore, in cases of the absence of the budget, budget revisions were no longer prepared as the changes would take an average of three months to be approved. As a result, Budget Holders/officers in charge of projects simply resorted to charging overtime expenses to other account codes.

217. We are concerned that expenses for overtime services were incorrectly reflected in the financial statements as these were inappropriately booked up in other expense accounts.

218. We recommend that the FAOR Laos (i) allocate the necessary budget for overtime services when preparing budget estimates; (ii) ensure the availability of funds before payments thereof; and (iii) use the appropriate accounts in recording such payments.

Procurement – Absence of PO Delivery Dates
(FAO Representation, Nigeria)

219. The facility to ensure the timely deliveries of goods and services need to be enhanced to promote their timely acquisition as a guarantee to effective and efficient use

of resources. This facility to establish accountability for timeliness of acquisition is built into the FAO Purchase Order (PO) which specifically requires the information on the dates on which the items ordered should be delivered.

220. The timeliness of delivery by the vendor forms part of his or her obligation and performance and validates the soundness of the way the contract was awarded to him or her. On the other hand, the absence of the date of delivery provides an excuse for the vendor in case he or she fails in his or her obligation and leaves FAO in a difficult position to claim for liquidated damages.

221. Results of our audits revealed the absence of delivery dates in the POs that would establish the explicit period within which the suppliers had to fulfil their obligations. In the case of the FAO Representation in Nigeria, where deliveries were completely effected 9 to 82 days from the dates of the POs, it could not be ascertained whether or not timely deliveries were complied with simply because there were no precise delivery dates to speak of in the first place.

222. Also, it is helpful to mention that liquidated damages could not be readily imposed without specifying the delivery date in the PO. If the contractor fails to deliver any or all of the goods or services within the period specified or at the quantity or quality specified in the contract for reasons other than force majeure, FAO may reject the goods in their entirety or in part and deduct liquidated damages from the total price of the goods a sum equivalent to 2.5 per cent of the contract price for each week of delay until actual delivery, up to a maximum of 10 per cent of the total price (Articles 19 and 20 of the General Terms and Conditions Applicable to FAO Procurement Contract).

223. Of utmost importance is the concern that the absence of delivery dates would somehow pose a risk that programme or projects may not progress as intended because the necessary inputs could not be delivered on time.

224. We recommend that Decentralized Offices consider implementing the requirement that the specific delivery dates be disclosed in Purchase Orders that will be served to the vendors and to which the vendors should agree.

225. We appreciate management's acknowledgement of the importance of the need to include the definitive dates for the deliveries of the goods ordered and that these be coordinated with the HQ and included as integral part of the procurement documentation.

PART IV

OTHER MATTERS

Write-Offs

226. Under Financial Regulation 10.4, the Director-General may, after full investigation, authorize the writing off of losses of cash, supplies, equipment and other assets, other than arrears of contributions. A statement of all such write-offs made during the financial period is to be submitted to the External Auditor with the final accounts. For

the biennium, there were five instances of write-offs reported involving USD 4.673 million.

227. Based on our audit, the write-offs were made in accordance with the prescribed procedures.

228. The Organization informed that no ex-gratia payments were made during the biennium.

Cases of Fraud and Presumptive Fraud

229. In 2008, two cases of submission of fraudulent claims for reimbursement of medical expenses were acted upon by the Organization, for which disciplinary action was imposed on a staff member. The respondent for the other questionable claim, a widow of a staff member passed away in 2009. Both cases were closed.

230. Also in 2008, the Organization dealt with and resolved two cases involving theft and attempted theft. Two staff members involved in the thievery cases were dismissed from the service while the temporary appointment of the staff member involved in the attempted theft was not renewed. Likewise, there were two cases of staff members providing and conveying false information to collect travel entitlement and for personal benefits. The staff member subject of the first case was dismissed while in the second case, the staff member was separated from the service and a note placed on her personnel file for future reference. All these cases had been closed.

231. In 2009, fifteen staff members and four former staff members were involved in the submission of fraudulent medical claims. Of the staff members, four were already dismissed while the cases of 11 were still under review. With respect to the former staff members, one and his family were removed from the ASMC plan and an administrative action was initiated on another for which some amount were recovered from his terminal emoluments. For the former staff member who could no longer be contacted, a note of her conduct was made a part of her personnel file for future reference. The case of the last staff member was still pending.

232. Furthermore, there were three consultants who were found to have committed various offenses, such as, defrauding the Organization through providing wrong information and failure to pay the suppliers, submission of falsified medical certificate prior to a second assignment and abuse of official position and dishonest representations to influence the procurement process. For the first case, the recovery of the amount defrauded is being assessed by the Legal Office. Notes were placed on the personnel file of the two other consultants.

233. For the above cases, USD 25,664.11 had been recovered and USD 43,060.30 were still being recovered. Total amount due for recovery was USD 90,199.41 (net of the amount of USD 4,110.31 which could no longer be recovered as the person concerned was not a staff member and already passed away in 2009).

234. The above cases were either the outcome of the investigation conducted by the Office of the Inspector General, Security Service and reports from the medical insurance company.

235. We have observed that appropriate measures were undertaken to resolve the cases, recover the amounts whenever possible and impose the appropriate sanctions.

Acknowledgement

236. We wish to express our appreciation for the cooperation and assistance extended to us by the Director-General and his staff.