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Interim report of the External Auditor, including the implementation of the recommendations of the External Auditor for the biennium 2006-2007; financial performance report and programme performance report for the biennium 2008-2009

Programme and Budget Committee

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Item 3 of the provisional agenda

Interim report of the External Auditor, including the implementation of the recommendations of the External Auditor for the biennium 2006-2007; financial performance report and programme performance report for the biennium 2008-2009

Interim report of the External Auditor

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For reasons of economy, this document has been printed in a limited number. Delegates are kindly requested to bring their copies of documents to meetings.



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OFFICE OF THE AUDITOR-GENERAL OF PAKISTAN
CONSTITUTION AVENUE
ISLAMABAD

16 March 2009

Dear Sir,

**Interim Audit report of the United Nations Industrial Development
Organization for the period 1 January to 31 December 2008**

I am privileged to present to the Industrial Development Board, through the Programme and Budget Committee, my interim report on the United Nations Industrial Development Organization for the period 1 January to 31 December 2008. The financial statements for the 12-month period of the biennium 2008-2009 ended 31 December 2008 have not been audited and no audit opinion is expressed thereon. In transmitting my report, I wish to inform that, in accordance with the United Nations Industrial Development Organization's Financial Regulations, I have given the Director-General the opportunity to comment on my report.

Yours sincerely

[Signature]

Tanwir Ali Agha
External Auditor
Auditor-General of Pakistan

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ACRONYMS

AH	Allotment Holder
BMS	Building Management Service
BPR	Business Process Reengineering
CTBTO	Comprehensive Test Ban Treaty Organization
CWT	Carlson Wagon lit Travel
DG	Director General
ERP	Enterprise Resource Planning
FPCS	Financial Performance Control System
FIN/FSB	Financial Services Branch
GES	General Support Service
HRM	Human Resource Management
IAG	Internal Audit Group
ICM	Information and Communication Management
IIA	Institute of Internal Auditors
IOS	Internal Oversight Service
IPSAS	International Public Sector Accounting Standards
ISA	International Standards on Auditing
ISACA	Information System Audit and Control Association
MD	Managing Director
NEP	Non Expendable Property
OSS	Operations Support Services
PCF	Programme Coordination and Field Operations Division
PM	Project Manager
PPE	Property Plant and Equipment
PSM	Programme Support and General Management Division
PTC	Programme Development and Technical Cooperation Division
RBM	Result Based Management
RFP	Request for Proposal
RFQ	Request for Quotation
SPT	Strategic Planning Team
TOR	Terms of Reference
UHO	UNIDO Head of Operations
UNGM	United Nations Global Market
UNIDO	United Nations Industrial Development Organization
UNOV	United Nations Offices in Vienna
UNSAS	United Nations System Accounting Standards
VBO	Vienna Based Organizations
VIC	Vienna International Centre
WCF	Working Capital Fund

1. INTRODUCTION

- 1.1 The UNIDO General Conference at its twelfth regular session assigned the External Audit of the United Nations Industrial Development Organization (UNIDO) for the fiscal period 2008-2009 to the Auditor General of Pakistan by resolution GC.12/Dec.15, 2007.

Audit Objective

- 1.2 The UNIDO's Financial Regulation 11.10 provides that "The report on the interim accounts shall be completed not later than by 1 June, following the calendar year to which it relates and shall be submitted to the Programme and Budget Committee." The practice of reporting in the interim year was first adopted in the 2002-2003 fiscal period. This report does not contain comments on interim financial statements which were under preparation at the time of audit in February/March 2009. The present audit was conducted for analytical review of selected operations of the UNIDO. As the fiscal period of UNIDO covers a Biennium, the attest audit of the Financial Statement will be carried out in March/April 2010 after the submission of the Financial Statements for the Biennium 2008-09 by the UNIDO.

Audit Scope

- 1.3 This Interim Audit Report covers the compliance with authority audit of the selected UNIDO operations and is based on the findings of the Strategic Planning Team (SPT) that visited the UNIDO Head Quarters during September/October 2008, and the audit findings of the Audit Team, which was in Vienna during February/March 2009.

Auditing Standards

- 1.4 The audit was carried out in accordance with Article XI of the Financial Regulations of UNIDO and the Additional Terms of Reference, governing the external audit, contained in the Annex thereto, as well as the International Standards on Auditing (ISA).

Audit Approach

- 1.5 To achieve our audit objectives, the audit teams reviewed selected programmes, projects, and activities with a view to ascertaining whether the organization had effective internal controls and had received value for money in its various operations.
- 1.6 The SPT visited the UNIDO headquarters with a view to documenting the administrative and financial systems. The team tested the validity of key administrative and financial controls on the basis of detailed internal control questionnaires. Financial Management, HRM, and Information Technology were the areas of focus. A review of procurement procedures, contracts, inventory, and asset management systems and practices was carried out for an assessment of the internal control environment prevailing in UNIDO. The team also reviewed the internal audit function and other work carried out by the Internal Oversight Services (IOS).
- 1.7 The Strategic Planning Team carried out an organization wide risk analysis and in this process benefited from the risk assessment conducted by the IOS for 2006-07. Based on the

risk assessment of the SPT, activities and operations with higher audit risk were identified for audit.

- 1.8 Following the road map prepared by the SPT, an audit team was deputed in February/March 2009 to carry out some substantive procedures and conduct analytical review of selected areas.

Reporting

- 1.9 During the audit, team members conducted interviews with the Director Financial Services Branch (FSB), Heads of various other branches and issued queries to the respective branches through the Office of Director FSB. This Interim Audit Report includes a number of observations and recommendations intended to be of benefit to the Organization. Response of the management to the Management Letter has been duly considered and appropriately reflected in this Interim Audit Report in an italicised form followed by further External Audit comments in bold letters.
- 1.10 The excellent cooperation extended by the UNIDO Management during audit is highly appreciated.

Observations

- 1.11 This Interim Audit Report for 2008 includes observations on the following areas of UNIDO operations:
- i. Internal Oversight Service
 - ii. Procurement of Goods and Services
 - iii. Management of Non Expendable Property (NEP)
 - iv. Management of the Travel Function
 - v. Human Resource Management (HRM)
 - vi. Operations in the Field
 - vii. Administration of the Working Capital Fund (WCF)
 - viii. Voluntary Renunciation of Unencumbered Balances of Appropriations
 - ix. Implementation of IPSAS
 - x. Financial Performance Control System (FPCS) – Agresso
 - xi. Outsourcing of Buildings Management Service (BMS)
- 1.12 A report on compliance of the previous External Auditor's recommendations in the light of management's response is also annexed to this Interim Audit Report.

Management Initiatives

- 1.13 The UNIDO management has undertaken a number of initiatives which include decentralization, outsourcing, sharing of common services by other UN organizations and Results Based Management (RBM). It is planned to review some of these areas including field operations during the next year and incorporate the findings in the final audit report for the Biennium. Besides, the project portfolio and investment management will also be examined.

2. INTERNAL OVERSIGHT SERVICE

- 2.1 The Internal Audit Group (IAG) Charter, issued in DG's Bulletin UNIDO/DGB (M).92/Rev.1 dated 8 November 2005, in line with UNIDO's Financial Regulation 9.1 and relevant Financial Rules, governs the working of Internal Oversight Service (IOS). As per the Charter, the mission of the IAG is to provide independent, objective assurance and advisory services designed to add value and improve UNIDO's operations by examining and assessing the Organisation's activities.
- 2.2 External Audit reviewed the status and working of the Internal Oversight Service (IOS) of UNIDO in the light of ISA 610. It was concluded that the IOS is working objectively; its personnel possess the required qualification and certification of various professional bodies, exercises due professional care and can freely communicate with the external auditors. However, the extent to which the management acts on the recommendations of the IOS was a matter of some concern as a number of recommendations had been outstanding for the last two years. Forty five percent of recommendations issued since 2003 have not yet been implemented.
- 2.3 The Audit noted that while the work programs and documentation existed, there was no single, consolidated internal oversight manual in the IOS which might serve as an institutional guide for the IOS.
- 2.4 During the Biennium 2006-07, IOS had issued 14 reports. The details may be seen from the following table:

Reports & Recommendations Issued during 2006-2007

Reports	Total Reports Issued	No. of critical Recommendations Issued	No. of Standard Recommendations Issued
Internal Audit	6	40	40
Investigation	5	5	2
Any other	3	0	0
Total	14	45	42

- 2.5 Of the 14 reports issued during 2006-2007, 6 were internal audit reports, 5 investigation reports, and 3 reports on the Joint Inspection Unit, comprising 45 critical and 42 standard recommendations. Five internal audit reports were issued in 2006. Only one report was issued in 2007 as most of the time was consumed in the development of an investigative report. IOS issued only one internal audit report in 2008.
- 2.6 The Audit observed that the IOS submitted all the reports to the DG who provided them to the parties concerned for necessary action. The system for follow-up of the recommendations was not well structured. The Head of the IOS maintained a list of recommendations for follow-up with the branches concerned, review of which revealed that implementation of IOS recommendations needed to be improved.
- 2.7 As per its Charter, the IOS was to submit an annual summary report on IOS activities. The Audit observed that no such report had been submitted for the last three years.

- 2.8 In terms of Rule 5.05 of the Rules of Catering Services at the Vienna International Centre (VIC), accounts of the catering Service shall be subject to audit by external and internal auditors of UNIDO who shall report thereon to the Director General of UNIDO. However, the Auditors noted that only a review of the Catering Service Contract was carried out in 2004. Since then Internal Audit of Catering Services had never been undertaken, due to paucity of resources.

Recommendations

- 2.9 With a view to increasing the effectiveness of the IOS in UNIDO, it is recommended that:
- i. An audit committee may be formed to examine the internal audit and investigative reports and monitor the implementation of recommendations of the IOS.
 - ii. Adequate resources may be provided, consistent with the Charter and workplan of IOS.
 - iii. Internal Oversight Manual of UNIDO may be developed in the light of international best practices.

Management Response:

Management has reported improved implementation of recommendations under the existing structure which will be verified by the External Audit. On the issue of IOS Manual, Management is of the view that ‘given the very different nature of IOS activities, i.e. internal audit and investigative ones, which are governed by different professional standards and due process requirements, it would appear of limited value to have a single comprehensive IOS manual encompassing both activities’.

On the issue of the activity report Management has indicated that due to other pressing engagements, activity reports could not be issued regularly.

Management has stated that the Catering Services was not a high risk area therefore its regular internal audit was not considered necessary.

Management agreed to examine the audit recommendation regarding constitution of Audit Committee in the light of position statement, “Audit Committees in the UN system and Multilateral Institutions”, which already stands presented to the High Level Committee on Management.

External Audit maintains that in line with the international best practices a manual containing all relevant rules, regulations, policies and procedures pertaining to Internal Audit function of the IOS may further help in institutionalizing the standardized practices.

IOS may align its activities with the Charter of IAG. Once the IOS resources improve, the internal audit of Catering Services may be included in the IOS workplan.

3. PROCUREMENT OF GOODS AND SERVICES

- 3.1 The Audit Teams carried out analytical review of the procurement process as well as a few selected contracts to assess systemic weaknesses and the Compliance with Authority during the process of acquisition of goods and services.
- 3.2 According to Paragraph 1.8 Chapter II of the Procurement Manual, Annual Procurement Plans shall be normally approved and issued by the Director PSM/OSS by 31 December of the year preceding the planning period. The Branch concerned could not provide to audit a copy of such plans. Absence of procurement planning may lead to lack of coordination, deprive the organization of the benefits of economies of scales, hinder long term and strategic planning and make monitoring difficult. Further, it may obstruct determination of organizational priorities for procurement.
- 3.3 Process of procurement was carried out manually and there was no centralized database for all procurement activities. The Auditors observed that there was no system of electronic approvals in place. Lack of automation may result in unnecessary delays, lack of synergy, non-sharing of expertise and knowledge, difficulty in trend analysis and monitoring, and non-availability of detailed data on procurement.
- 3.4 Paragraph 104 of the Procurement Manual indicated that intranet-based headquarters procurement planning system was scheduled for development in 2008. The management informed that there was no development of the system during 2008.
- 3.5 UNIDO advertises procurement opportunities on its website and also directly invites potential bidders to participate in the competitive process. The Audit observed that bidders were generally not very responsive to UNIDO procurement and very few bidders participated in the process. The management needs to analyze the causes as this trend may lead to limited competition with all its attendant risks.
- 3.6 As part of the analytical review of the contracts for procurement of goods and services, a sample was drawn from the population of contracts and tested for compliance with authority and regularity. The details of the review were brought to the notice of the Management through the Management Letter. While the overall process of contracting was found to be generally compliant with the regulatory framework, some of the issues that needed Management's attention were:
- repeated waivers from open competition
 - limited competition
 - discretion in defining the number of suppliers for RFQs
 - inadequate terms of reference for procurement of goods and services
 - lack of comprehensive and quantifiable specifications, and
 - splitting of contracts to invoke waivers from international bidding.

Recommendations

- 3.7 On basis of the analytical review, it is recommended that:
- i. Annual Procurement Plan may be prepared and approved within the time limit stipulated in the Procurement Manual.

- ii. Procurement function may be computerized with a centralized database for all procurement activities. It may also be linked with Agresso throughout the process. System of electronic approvals during the procurement process also needs to be institutionalized.
- iii. Process of recruitment for the position of Chief of Procurement, vacant since November 2007, may be completed expeditiously.
- iv. Repeated waivers on the grounds of proprietary and standardization may be discouraged.
- v. Market research/surveys may be conducted to identify competent and technically qualified bidders to ensure that enough bidders participate in the competitive process. At the time of identifying suppliers from the Suppliers' Roster of UNGM, efforts may be made to shortlist vendors with a reliable track record in terms of responding to the bids and actual delivery of supplies.
- vi. Procedures in the Procurement Manual need to be geared to limit the discretion of Procurement Officers in defining the number of suppliers for "Request for Quotation", and for the finalization of the list of suppliers, in case of limited solicitation.
- vii. If a contract is to be awarded that involves future phases as well, this fact should be clearly mentioned in the solicitation documents to ensure equal opportunity and level playing field for all bidders.
- viii. UNIDO has started procurement training for staff in 2008 followed by an on line test. It is recommended that only those officers be allowed to undertake procurement activities who qualify the test.
- ix. For all acquisitions, neutral, clear and preferably performance oriented specifications should be determined, in line with the provisions of Paragraph 3.1, Chapter 2 of the Procurement Manual, so that the goods and services procured match the actual requirements of the organisation. Due care should be exercised in defining the deliverables of contracts so that all the requirements are converted into measurable outputs.
- x. Financial evaluation should be carried out by the authorised officials only.
- xi. In case of advance payments appropriate guarantees must be obtained.

Management Response

The Management duly noted the audit findings and generally agreed to the recommendations.

External Audit appreciates efforts to improve the procurement process and will continue to monitor the developments in this regard.

4. MANAGEMENT OF NON-EXPENDABLE PROPERTY

- 4.1 As per the accounting policy of UNIDO, expenditure on acquisition of furniture, equipment, other non-expendables and leasehold improvements is charged to expenditure in the year of purchase and is not included in the assets of the Organization. The inventory of such non-

expendable property is maintained on historical cost basis and the value is disclosed in the notes to the financial statements.

- 4.2 Documentation of the value of equipment and other property purchased, and the projected serviceable life span of each asset, is an important control over the physical assets of an organisation. The Audit observed that in UNIDO the record of the property maintained by the General Support Services Unit (GES) did not have any interface with the financial records maintained by the Financial Services Branch. In effect, it means that under the existing system there were insufficient controls to ensure that all the acquisitions which were acquired during a financial period, as per the record of the Financial Services Branch, were actually taken on the inventory lists of the GES. The international best practices in this regard suggest that all the inventories of physical assets should be based on the financial information available in the books of account. They also suggest that there should be a periodic reconciliation between the financial records maintained by the accounts section and the inventories maintained by the managers of the assets.
- 4.3 The Audit observed that the Finance Branch did not have a system of reconciliation between the accounting record pertaining to procurements and the record of non-expendable property and special items maintained by the GES. The Finance Branch, informed the audit team that “new additions to NEP are recorded as ‘acquisitions’ in the accounts, but as it is fully expensed, it is not reconciled to the fixed assets register. The information on NEP is provided by GES for the financial statements.” In the absence of a reconciliation regime between the financial records and the inventories of physical assets, it is difficult to ascertain that the value of the non-expendable property and special items reflected in notes to the financial statements is based on the actual financial records of the acquisitions.

Recommendations

- 4.4 In view of the above it is recommended to ensure that:
- i. The accounting records provide adequate classified information on all acquisitions.
 - ii. The accounting information on physical assets is used for developing inventories of physical assets.
 - iii. There is periodic reconciliation between the financial record of assets and the physical inventories.
 - iv. Physical verification of the NEP is conducted with reference to the central accounting record maintained by the Finance Branch.

Management Response

While agreeing to the best practice as stated by the External Auditor the Management felt that other compensatory measures were in place. However, the adoption of IPSAS will eliminate the weakness pointed out by Audit.

External Audit will continue to follow up on the developments.

5. MANAGEMENT OF THE TRAVEL FUNCTION

- 5.1 UNIDO provides for worldwide travel of its headquarters and field staff, including technical assistance project personnel, upon recruitment, transfer, separation, official business and home leave, as well as education grant travel for the staff members' dependents. In addition, the Organization provides for the travel of delegates from Member States attending their meetings in Vienna, participants attending conferences and expert group meetings, as well as other persons on official business, as and when required by the Organization. Total expenditure on Travel during the year 2008 amounted to €4,127,908.
- 5.2 Travel, Transportation, Visa and Shipment Unit within the General Support Services (PSM/OSS/GES) is responsible for providing essential services in support of all UNIDO activities and acts as liaison between UNIDO and the travel agent to ensure that the relevant entitlements and regulations are observed. As part of this monitoring function, the travel unit checks the fares and itineraries provided by the travel agent to ensure that they are in line with UNIDO travel policy. Any divergence is required to be immediately brought to the attention of the Travel Agent.
- 5.3 Following repeatedly unsuccessful competitive bidding exercises, UNIDO entered into a negotiated contract with Carlson Wagon lit Travel (CWT), Austria, who were already providing services to UNOV and CTBTO. The contract was signed w.e.f 1 March 2004 through 30 June 2006 for an initial period of two years and four months, with an option to extend for a further two years. As per the Contract, "UNIDO shall pay to the Contractor the agreed flat rate (or less) of € 60 per air ticket and € 15 per rail, car, hotel, and steamship transaction and fares (s) for each journey and services." Upon enquiry the Auditors noted that there was no documentary evidence available in the Unit as to the process for entering into the negotiated contract with CWT.
- 5.4 In October 2008, UNIDO, UNOV, and CTBTO signed a joint contract with CWT for an initial period of eighteen months with the provision for two optional extensions after a competitive bidding exercise. As per the contract, the transaction fee shall be €53 per airfare transaction and €15 per Other Transaction.
- 5.5 Article 2.2.22 of the 2004 contract provided for a quality control system under which the contractor was required to conduct a quarterly customer satisfaction survey and suggest action plans to address any issues emerging there from. Neither the Contractor complied with this contractual obligation nor did the Travel Unit follow it up.
- 5.6 UNIDO, however, on its own conducted a customer satisfaction survey in March 2006 on the performance of CWT which incidentally was not representative as the number of responses was very low. Majority of respondents were generally satisfied with the performance of CWT. However, some respondents recommended CWT to have more pro-active client oriented approach, improve its knowledge of connection time and routing, adopt innovative approach, and offer more competitive prices for private travel. Overall results of the survey established that CWT needed to improve its performance.
- 5.7 In order to assess the efficacy of the service provider, the audit team designed a customer satisfaction survey which was administered to 15 top travellers. The survey responses revealed that the users were broadly satisfied with the range of services provided by the travel agent. However, there was room for improvement in the following areas:
- explanation of airfare rules and restrictions by the Travel Agent to UNIDO personnel

- recommendation for appropriate lodging for the travellers
 - accurate lodging reservations for travellers
 - recommendation for appropriate ground transportation to the UNIDO personnel
- 5.8 It was noted that in certain cases the Travel Unit had been proposing changes to the itineraries suggested by the travel agent because they were not based on the most direct and economical routes as required under the contract. Such proposed changes resulted in significant savings to UNIDO. The available record for 2008 showed that in 15 cases there was a saving of 31% as against the prices quoted by the Travel Agent. While the credit for these savings goes to the Travel Unit, it was noticed that there was no systematic method of maintaining record of such savings. It may be a consideration of merit for the Travel Unit to develop a regular performance monitoring framework of the service provider.
- 5.9 In accordance with Amendment A to the 2004 Contract signed on 3rd August 2006, “A reduction of €2.5 per transaction will be granted for payments of monthly invoices processed within 30 days after their receipt and acceptance”. The Contractor also agreed to pay back the super commission to UNIDO, “The Contractor shall credit super commissions against invoices within the first quarter of the year for the preceding calendar year”. The Audit observed that the Contractor did not timely fulfil this contractual obligation. Similarly the 2008 contract also provided for a rebate of at least €2.50 per airfare transaction and a super commission of at least 1.25 percent of the total air fare transaction to be reimbursed at the beginning of the next calendar year. Neither the rebate nor super commission had yet been paid by CWT to UNIDO for 2008. Travel Unit needs to work out the receivable amount and get it credited to the UNIDO’s account; and for future, establish a mechanism for timely action in this regard.
- 5.10 According to Terms of Reference of the 2008 Contract “The contractor shall arrange, at no additional charge, the refund of unused refundable tickets within 30 to 60 days of submission, as well as the replacement of all lost or stolen tickets or coupons. The contractor shall provide a monthly report of status of refunds and claims”. It was observed that CWT was not providing monthly report of status of refunds and claims. Some refund cases of June 2008 onward were found outstanding.

Recommendations

- 5.11 In view of the above it is recommended that:
- i. In the Travel Unit, a performance measurement system may be instituted to regularly and effectively evaluate the performance of CWT.
 - ii. Travel Unit needs to ensure that all refunds/rebates, credits and reports are received within the time limits specified in the contract.
 - iii. As provided in the TOR of the contract, a third party Point-of-Sale audit of airfares may be carried out.

Management Response:

The Management generally agreed to the recommendations of the External Audit. Further, they informed that in line with the recommendation of the External Auditor ICM will be

approached with the request to automate this process using the functionalities of the Travel System.

Regarding collection of discounts for timely payments of invoices and credit of super commissions, the Management informed that the collection for timely payment will be received by UNIDO in March 2009 and the credit for super commission by the end of May 2009. UNIDO in cooperation with other VBOs and the Travel Agent will establish realistic schedule for receiving the refunds and, if required, the contract will be amended accordingly.

Subsequent External Audit teams will verify the receipt of refunds, the amendments in the contract, and the improvements to the monitoring of travel operations in UNIDO.

6. HUMAN RESOURCE MANAGEMENT

- 6.1 Short term appointments are to be resorted to, under the management policy in exceptional and specific circumstances. During 2008, 75 short term appointments were made by the management. Out of these, 31 appointments were made against fixed term posts. The management explained that these appointments have been made to “bridge” the gap while recruitment was in process. In some other cases, managers had to resort to short term recruitment as long term recruitment was not allowed due to lack of confirmation of funds against regular budget posts. Still in other cases, it was used for positions funded from project funds as a saving measure due to insufficient project funds for long term recruitment.
- 6.2 UNIDO’s existing policy on staff development, training and learning is contained in Annexure-V of the DG’s Administrative Instruction No.10 dated 19th February 2001. Another proposed Policy on Learning has been prepared which is reportedly under discussion at the Joint Advisory Committee.
- 6.3 A comparison of the list of Learning Areas as described in the above mentioned two policy documents showed that the proposed Policy on Learning had identified new learning areas. The titles of the learning areas indicated that efforts had been made to take into account the issues resulting from structural re-organization and provided an opportunity to the staff to acquire knowledge and skills for handling these issues. Existing Training Policy document obligated the respective Managing Directors to establish an annual divisional training plan in the last quarter of each year for the following year.
- 6.4 The External Audit observed that:
- Existing policy document was flexible enough to allow the Managing Directors to make adjustments, within allocated financial resources; by way of inclusion of any training requests for their staff including requests unforeseen at the time of preparing the annual plan that were consistent with the approved training policy.
 - Proposed ‘Policy on Learning’ did not prescribe any timeline for the HRM Branch to finalize and submit the training plan to the Director General.
 - Flexibility was missing in the proposed Policy on Learning.
 - Delay in finalization and approval of the annual Learning plan 2008 had watered down the purpose and spirit of the planning exercise.
- 6.5 The DG’s Bulletin No. UNIDO/DGB/(0).95/Add.4 dated 29 February 2008 announced the establishment of the Office of Ombudsperson with a direct reporting line to the

Director-General. It is supposed to provide an informal conflict management and resolution facility for UNIDO staff. The Bulletin also stated that the terms of reference for this position were being finalized through consultation between management and staff within the framework of the Joint Advisory Committee. The Terms of Reference were finally approved by the Executive Board on 21 January 2009. The ToRs provided the guiding principles about the conduct of business by the Ombudsperson and the staff, as well as the qualifications and the selection process for the incumbent. These were, however silent about the classification of the post.

- 6.6 Early finalization of the process is emphasized so that the office which, according to the bulletin stands established in February 2008 should become functional at the earliest.

Recommendations

- 6.7 In view of the above analysis it is recommended that:
- i. While resorting to short term appointments, care should be taken that practice does not contraindicate policy on the subject, and the commitment, responsibility and accountability that come with longer fixed term appointments may not be compromised.
 - ii. Appropriate timelines for finalization and submission of Annual Training Plan may be incorporated in the proposed Learning Policy.
 - iii. Adjustments in the Annual Training Plan may be provided for in the proposed policy so that the flexibility available in the existing policy is retained.
 - iv. On-line courses be developed and delivered for the field office staff.

Management Response:

The Management has taken note of the auditors' recommendations regarding short term appointments and has agreed to monitor the utilization of short-term appointments so as to ensure that it is in line with the existing policy.

The Management has also agreed to amend the draft policy in line with audit recommendations.

The Management stated that the appointment of the Ombudsperson will be considered in the context of available resources and priorities.

Subsequent Audit teams will verify the amendment in the policy.

7. OPERATIONS IN THE FIELD

- 7.1 Currently 1,396 UNIDO projects valuing US\$ 621.72 million are operational in 121 countries. While most of these projects are funded by the voluntary contributions from the Member States under the Technical Cooperation Assistance, some are also funded under the operational budget of UNIDO. With a view to ascertaining the efficacy in the management of these projects the audit teams carried out a short study of the project management and financing arrangements for this core activity of the Organization. It was

observed that an internal control mechanism existed in UNIDO headquarters to ensure sufficient involvement of the HQ in the project execution.

- 7.2 Under the Decentralization initiative, measures have been introduced for delegation of authority to enable Project Allotment Holders (AHs), UNIDO Representatives (URs) and UNIDO Heads of Operations (UHOs) to meet the requirements of the technical cooperation projects and field offices for procuring services and goods of a limited value in a prompt and cost-efficient manner. These are consistent with the principles of accountability and transparency as encoded in the Financial Regulations and Rules of UNIDO. Deployment of appropriate human resources is always critical for effective implementation of projects and programmes, and it is felt that the field offices of UNIDO are better placed in identifying suitable personnel to meet the challenges of indigenous circumstances.
- 7.3 An on-going Trust Fund project was reviewed by the External Audit on the basis of the information available at the UNIDO Headquarters. This project was aimed at assisting the concerned country in its endeavours for recovery and rehabilitation of the manufacturing industry and the development of the private sector after the war period, to fit within the globalized world market. The Project was approved in November 2000.
- 7.4 The Project Manager, who is the Allotment Holder for the Project, informed the audit team that the RBM reporting of the Project was not done as the Project Document had been prepared before the introduction of RBM and no provision for reporting on RBM was made in the document. Besides the National Project Coordinator was working on part time basis and did not have the knowhow of the RBM.
- 7.5 Out of the fifteen project objectives, three had been achieved fully, six had been achieved partially and the rest could not be achieved at all. The limited capacities of the cooperating institutions in the public and private sector were identified as the most serious risks for the achievement of the project objectives. However, it was assessed that the risk was minimised by focusing on institutional capacity building.
- 7.6 It is appreciated that the project has been partially successful in aiding the concerned country in its endeavours for recovery and rehabilitation of the manufacturing industry and the development of the private sector after the war period. It is also recognised that managing the identified and unidentified risks involved in implementing such projects is always a challenge.
- 7.7 Selection of appropriate HRD intervention is a critical factor for the projects involving indigenous HR input. Greater value for money could have been achieved, for both the donors and recipients of the aid, if the Project was successful in creating a critical mass of qualified national expertise in the target areas through appropriate human resource development strategy.

Recommendations:

- 7.8 It is recommended that:
- i. While implementing the decentralization initiative the operational requirements of the field offices may be kept in view so that speedy and effective implementation of projects and programmes is ensured.
 - ii. For implementing such projects in future, it may be advisable to consider deployment of some resources as well as expertise, both indigenous and international, for identifying

workable Human resource Development Strategy which is likely to be successful in the cultural and political milieu of the target country.

8. ADMINISTRATION OF THE WORKING CAPITAL FUND (WCF)

- 8.1 UNIDO activities are financed by annual assessed contributions from the Member States as well as voluntary contributions. Based on the estimation of assessed contributions and voluntary contributions, the regular and operational budgets of UNIDO are approved by the General Conference for a Biennium. While the expenditure of UNIDO can be forecast on the basis of the approved activities, the receipt of contributions remains uncertain. Situations may arise when the Member States do not pay their contributions on time.
- 8.2 In the perspective of such financing arrangements, there seems to be a need for bridge financing the programmes in situations when some of the financial resources against which programmes are budgeted are not available during the fiscal period. Theoretically, such bridge financing arrangement is available in the form of the Working Capital Fund as stipulated in Regulation 5.1. However, it appears that the management of UNIDO has never felt confident about using the fund for bridge financing because of certain perceived constraints in its utilization.
- 8.3 In accordance with Financial Regulation 5.4, the General Conference established the Working Capital of UNIDO to the tune of US\$ 9,000,000 in its first session in December 1985 (GC.1/Dec.33) and authorized the DG to finance from the fund such sums as may be necessary to finance budgetary appropriations pending the receipt of contributions. The level of the Working Capital Fund has been kept at € 7.4 million since the Biennium 2002-2003, which is sufficient to meet the requirements of UNIDO for two and a half months.
- 8.4 The UNIDO management is obliged to replenish the withdrawals from the WCF within the same fiscal period in which the withdrawals are made. Financial regulation 5.4 (c) lays down that advances made from the Fund to finance approved regular budget appropriations shall be reimbursed as soon as and to the extent that contributions or advances from Members are available for that purpose and in terms of the Financial Regulation 5.5 (c) payments made by a Member shall be credited first to the Working Capital Fund and then to the contributions due, in the order in which the Member was assessed.
- 8.5 UNIDO management stated they could never be sure of the fact that they will receive enough receipts to reimburse the withdrawals from the WCF. As a result, the management has virtually never used the WCF for its programme activities even in years they have not received adequate contributions from the Member States. Consequently, the budgeted programmes are exposed to implementation risk.
- 8.6 External Audit observed that during the years 2002-07, the collection rate of assessed contributions ranged from 89.8% to 93.7%. As the programme activities of the organization are budgeted and planned against projected income, late receipts of assessed income may impact the materialization of the programme, since UNIDO does not resort to utilization of WCF, despite the fact that it is not necessarily cash starved.

Recommendations

- 8.7 In view of the above, it is recommended that:

- i) Ceiling of WCF may be fixed at a level that late receipt of contributions may be accommodated.
- ii) Suitable amendment may be made in the Financial Regulations to allow the UNIDO management the flexibility to replenish the withdrawals from the WCF in the 12 months period following the fiscal period in which the withdrawal was made.
- iii) The management may like to consider the option of utilizing the WCF to bridge finance late collection of assessed contribution.

Management Response:

The Management responded that they utilized the WCF in December, 1995, 1996 and 2004. While in 2004 the WCF was replenished in the following year from the proceeds of supplementary assessment, in 1995 and 1996, it took some years to replenish the fund to the approved level. Hence, for prudent financial management, the Organization attempts to keep the expenditure to the level of collection of assessed contributions, thereby retaining the WCF to fund unforeseen events.

The Management did not agree with the recommendation to utilize WCF for bridge financing on the grounds that the WCF once used up in a Biennium, would need to be replenished immediately by Member States as part of the next assessment cycle in order to allow a repeated use in the following year.

It is not clear whether the Management desires to use the WCF for the purposes specified in Regulation 5.4 (c), which provides that the WCF may be used to finance the approved regular budget appropriations. If the WCF cannot be used to finance the temporary shortfalls in the receipt of assessed contributions, then the Management needs to clarify the purposes for which the WCF was created. The External Audit will review the issue at the time of the finalization of the report for the Biennium.

9. VOLUNTARY RENUNCIATION OF UNENCUMBERED BALANCES OF APPROPRIATIONS

- 9.1 In its 12th session in December 2007, General Conference encouraged the Member States to “Consider voluntarily renouncing their share of the unencumbered balances of appropriations to support UNIDO activities in areas such as:
- i. Enhancement of field representation;
 - ii. Promoting increased coherence in its areas of work, including coordination of the United Nations Energy Group;
 - iii. Youth employment in productive activities;
 - iv. Follow-up on issues arising from the Ministerial Conference of the Least Developed Countries;
 - v. South-South cooperation;
 - vi. Regional programmes;
 - vii. Any other purpose to be specified by the Member States”. (GC.12/Dec.10 Financial Situation of UNIDO)

- 9.2 An amount of €8,891,000 was available in unencumbered balances of appropriations on 31st December 2007. In response to General Conference decision to request renunciation, Ireland, Mexico, Portugal, Thailand and the UK renounced an amount of €757,247 by 30th June 2008.
- 9.3 The General Conference had been taking similar decisions in the past, as well. When General Conference took this decision in December 2007, (GC.12/Dec.10), the point regarding any other purpose to be specified by the Member States, was added to give an additional option to Member States in case the six specific options mentioned were not suitable to some of them. The scope/restriction would be limited to UNIDO activities as specified in the opening paragraph. Contributions were treated in accordance with the purpose for which renunciation was made, i.e. special purpose/donor contributions.
- 9.4 In case of Ireland, Mexico, Portugal and Thailand no projects have yet been established and as such no expenditures have yet been incurred. In case of the UK, funds have been further allocated for a specific purpose of utilization for strengthening fiduciary standards and placed under project number TEGLO08015.
- 9.5 The positive response from the Member States will contribute to UNIDO activities in various areas after projects have been identified. It may also help to reinforce UNIDO's resource position and enable it to carry out its reform/modernization initiatives.

10. IMPLEMENTATION OF IPSAS AT UNIDO

- 10.1 At its 60th Session in July 2006, United Nations General Assembly approved the adoption of International Public Sector Accounting Standards (IPSAS) throughout the UN System by 2010. In compliance with this UN decision, process of obtaining approval of UNIDO Governing Bodies was initiated in November 2006 that culminated in December 2007 when the General Council, at its twelfth session, decided to adopt IPSAS at UNIDO, effective 1st January 2010, as part of the UN System wide adoption of these standards.
- 10.2 A working group in the Financial Services Branch was established in February 2007 to address critical issues related to adoption of IPSAS. Under the working group, sub-groups were established for Property, Plant, and Equipment (PPE), Revenue recognition, Employee benefits, and Intangible assets. An IPSAS Implementation Task Force was established in April 2008 to execute and monitor the overall process of IPSAS implementation at UNIDO.
- 10.3 A note presented to the IDB vide Document IDB.33/5–PBC.23/5 dated 23rd March 2007 identified the areas likely to be affected by the decision of implementation of IPSAS and also spelled out action plan 2008-2009 for implementation of IPSAS by UNIDO.
- 10.4 The Audit reviewed the implementation of action plan for 2008-2009 and observed that though some headway had been made, some activities were behind schedule. However, UNIDO management believed that it was on track for implementing IPSAS with effect from the target date i.e. 1st January 2010.

Recommendations

- 10.5 It is recommended that:
- i. IPSAS implementation may be accorded priority. Management needs to ensure that resource constraints do not hamper IPSAS implementation.

- ii. Specialists be hired and dedicated to undertake the task of IPSAS implementation on a full time basis, to streamline and facilitate the implementation process.

Management Response:

The Management's response to the review conducted by the External Audit in terms of milestones and progress achieved is presented at Annexure 2.

Being an important area, the subject will remain under review.

11. FINANCIAL PERFORMANCE CONTROL SYSTEM (FPCS) – AGRESSO

- 11.1 UNIDO started implementation of a few selected modules of Agresso, a commercial Enterprise Resource Planning (ERP) System, in April 2000. The system went live on 1st January 2002.
- 11.2 In order to measure the existence and effectiveness of General and Application Controls in the FPCS-Agresso, audit developed questionnaires for seeking responses from Information and Communications Management (ICM) Branch, Accounts and Financial Reporting Group, Payments Group, Treasury Group, Payroll Group, Budget Group and FMT Unit.
- 11.3 Responses to the Audit questionnaire indicated:
 - Some deficit in understanding the Information System Business processes, by the staff that has been working on these processes since long.
 - Lack of clarity about the ownership of various Financial and Information System processes.
 - Lack of segregation of duties in the Information and Communication Management (ICM) Branch.
 - Weak data input controls.
- 11.4 Various walkthrough tests by the audit team revealed that use of FPCS, by and large was limited to financial data only. It did not support HR or Procurement functions in planning and decision making. The Agresso generated list of “Contracts Awarded During 2008” for audit was silent about the method of procurement (other than waiver), and the effective date of the contract. On enquiry it was communicated that being non financial information, Agresso did not capture this information at the time of registering the Purchase Requisition and hence it could not be generated.
- 11.5 Response to verbal enquiry revealed that the FPCS was not being used to generate the annual financial statements.
- 11.6 Audit is of the view that given the capability of the software, Procurement and Fixed Assets Modules could have been utilized more effectively by creating interfaces between these modules and the Accounts and Payments Modules for making it available to a number of users for better planning, monitoring and reporting. The Audit noted that the System Administrator was placed in the Financial Services Branch, whereas, the overall responsibility of the maintenance of the IT systems rested with the ICM Branch.
- 11.7 UNIDO is making preparations for implementing an up-graded version of the ERP system Agresso by 1st May 2009. This poses dual challenge of simultaneously going through “run the

business” and “change the business” scenarios. Owing to change in the basis of accounting from UNSAS to IPSAS, the complexity and gravity of the situation is increased and the organization becomes exposed to high levels of risks. ERP system implementations can fail to deliver expected results if not adequately managed and controlled. It is opportune to draw the Management’s attention to the following risks, listed by the ISACA IS Auditing Guidelines:

- “The changes proposed by a BPR may require the people affected to behave in a different manner and may engender support, concern and/or even hostility within an organisation. This may be transferred to the ERP implementation project.
- The BPR may drain organisation resources from the ERP implementation.
- Even if the above two risks have no effect on the ERP implementation, unfamiliarity with new processes introduced by the BPR might lead to inadequate process description and suboptimal configuration of the ERP.
- The BPR and ERP may not be well integrated leaving, at best, suboptimal performance and unnecessary expenses.
- Using an ERP as a “change lever” may distract from the BPR. With new, more powerful technology there is a temptation to adopt a process simply because the new technology “can do it,” rather than because it is the optimum business process.”

Recommendations

11.8 In view of the above it is recommended that:

- i. Before migrating to the new version of the FPCS, the business processes and the system requirements under IPSAS may be carefully defined to avoid the risks identified in para. 11.7.
- ii. Improved coordination between the ICM and the FIN Branches may be ensured for successful transition to new systems.
- iii. The roles and functions of ICM and substantive branches with regard to system design, development, operations, and maintenance may be defined clearly for optimal utilization of the IT systems.

Management Response:

The Management attributed the lack of understanding of the system to limitation of staff resources.

The Management also stated that all data required for preparation of annual financial statements are extracted from FPCS.

At the time of the Agresso purchase the decision was to use it mainly for financial purposes. The upgrade will allow some process reengineering especially with reference to IPSAS. The Management stated that the testing of the new business processes on Agresso could not be undertaken simultaneously. Some of the new business processes were being tested while some others were still under development.

External Audit maintains that the data still has to be tabulated as a secondary exercise in the current arrangements and the system is unable to generate the Financial Statements directly.

Migration to the new systems needs to be closely supervised for mitigating risks and ensuring value addition by the new system.

12. OUTSOURCING OF BUILDING MANAGEMENT SERVICE

- 12.1 Building Management Service (BMS) of UNIDO is mandated to carry out all civil, mechanical and electrical works for the VIC. Its budget is financed by the VBOs according to a pre-defined cost allocation key. In case of the Major Repair and Replacement Fund (MRRF) the Government of Austria finances 50% of the funding.
- 12.2 In 2008, the Committee on Common Services in consultation with the VBOs hired a consulting firm to carry out an assessment of Common and Joint Services of the VIC. Regarding BMS the consultant recommended a two pronged strategy; implementation of an efficient Project Management and Tracking System which will help increase efficiency followed by re-organization ultimately leading to outsourcing of the service.
- 12.3 The consultant's report did not address all the issues for enabling the management to take a prudent decision towards the BMS outsourcing. Cost elements such as the expected costs of outsourcing contracts and separation benefits to the employees to be laid off as a result of outsourcing have not been calculated by the consultant.
- 12.4 In order to make an informed decision on outsourcing, the management would need an impartial and transparent proposal based on well constituted ToR. A holistic view of the issues involved is required.
- 12.5 The proposal for outsourcing the BMS, needed to be measured against UN Resolution 55/232 of December 2000 on outsourcing practices. The Resolution vide paragraph 1 requests the Secretary-General to continue to ensure that program managers are guided by the following four basic reasons for outsourcing:
- (a) To acquire technical skills not readily available within the organization, including accessing state-of-the-art technologies and expertise or acquiring needed flexibility to meet quickly changing circumstances;
 - (b) To achieve cost savings;
 - (c) To provide a service more effectively, efficiently and expeditiously; and
 - (d) To provide an activity or service not needed on a long-term basis;
- 12.6 Due consideration needed to be given to the reports of Joint Inspection Unit of UN, which have consistently emphasized that safety and security, and maintaining the international character of the organization might be kept in view while taking decisions on outsourcing.

Recommendations

- 12.7 In view of the above, it is recommended that:
- (i) Overall cost-benefit analysis covering all the cost elements including the one time and recurrent costs may be carried out.

- (ii) The key elements of UN outsourcing policy as well as a workable formula to distribute the service provider's charges among the beneficiaries (VBOs) may be kept in view for moving towards outsourcing the BMS.

Management Response:

The Management has noted the recommendations of the External Audit and informed that it is in the process of obtaining services of an independent outsourcing expert for conducting additional cost-benefit analysis.

Implementation Status of IPSAS

Activity	Target Date	Present Status as of 16 th Feb 2009	Activities behind schedule	Management Response
Completion of Fixed Assets related activities	June 2008	Partially completed	<ul style="list-style-type: none"> Final decision on the method of initial valuation of assets has not yet been taken 	<p><i>In 2008, a set of accounting policies for PPE were recommended by the Sub-Working Group on PPE and approved by the IPSAS Working Group. A policy on the initial valuation of PPE was also adopted, i.e., to use Fair Value as at the date of recognition. However, taking into account the cost involved, a more practical way was found to consider cost as at the date of acquisition as a more cost effective method. Data has been collected to analyze the availability of source documents and is in the process of final analysis. This activity is scheduled for completion by mid-March.</i></p>
			<ul style="list-style-type: none"> Verification/recording of Head quarters (regular budget) Property, Plant and Equipment (PPE) has not been completed yet. 	<p><i>The physical verification of regular budget Headquarters assets is almost complete, except for assets of Buildings Management Services (BMS), which has been constrained by the Asbestos removal project at the Vienna International Centre, but is due for completion by the first quarter of 2009.</i></p>
			<ul style="list-style-type: none"> PPE process flows for Head quarters regular budget have not yet been finalized 	<p><i>The IPSAS-compliant work flow processes have been designed and sample tests are being conducted in the system to enhance the monitoring of the entire process of asset management, from acquisition to disposal. The testing has not been completed yet because holistic system testing will be continually conducted throughout 2009.</i></p>

Activity	Target Date	Present Status as of 16 th Feb 2009	Activities behind schedule	Management Response
			<ul style="list-style-type: none"> • Identification of Field Office assets (regular budget) has not yet been completed 	<p><i>In December 2008 as part of the year-end closure exercise, a survey was transmitted to the field offices seeking confirmation from each field office of the existence of a list of assets per field office extracted from the fixed asset register maintained at Headquarters. This confirmation is undertaken on an annual basis. The main objective was to seek confirmation once again from each field office of the existence of each asset contained in the list of assets extracted from the fixed asset register; to obtain information on assets, which was not included in this list; to obtain information on contributions in-kind and leases. To date, completed surveys have been received from 30 field offices and ITPOs. The survey results have been analyzed and field office assets are being updated, where necessary.</i></p>
			<ul style="list-style-type: none"> • Policies/processes on Technical Cooperation assets have not yet been developed and UNIDO intends to use transitional provision for five years to streamline the policy on TC assets. 	<p><i>A set of general accounting policies for PPE, including preliminary review of TC PPE policies, along with suggested subgroups and useful lives, which were developed in 2008 are currently under review. The process flows for TC assets is currently under development and will be completed in 2009. The acceptance of transitional provisions, allowed under the Standard on PPE (IPSAS 17), provide time for implementation.</i></p>
			<ul style="list-style-type: none"> • Formula for including the percentage of VIC building in assets has not yet been arrived at. 	<p><i>This activity was dependant on the finalization of the recommendations of the Consolidation project conducted by the UN as the lead agency. Deloitte was tasked with this work. It has recently been confirmed by the UN that their report is final. Discussion has commenced with IAEA on VBO issues related to Common Services to develop harmonized policies and business processes in the area of Consolidated Financial Statements/Interests in Joint Ventures.</i></p>

Activity	Target Date	Present Status as of 16 th Feb 2009	Activities behind schedule	Management Response
			<ul style="list-style-type: none"> Inventory management system not yet finalized 	<p><i>After review of all existing inventories at UNIDO the decision has been taken to expense publications, the library and office supplies of stationary since their value did not prove to be material. Consequently, it has been moved down from a high priority activity in 2008. On account of limited applicability for BMS and Catering, it was decided to take it up only in 2009 when the Agresso system upgrade, which has an inventory module, will be installed.</i></p>
			<ul style="list-style-type: none"> Business processes for inventory management not yet developed/ analyzed 	
			<ul style="list-style-type: none"> Policy paper on intangible assets not yet finalized 	<p><i>A survey on identification of intangible assets, along with their parameters of recognition and measurement criteria carried out at UNIDO headquarters, Field Offices, ITPOs, etc. in 2008 indicated limited assets under this category. Policy on accounting for UNIDO's Intangible Assets, mainly for identification and recognition has been developed by Finance and will be finalized shortly.</i></p>
Accounting for obligations, support costs, employee liabilities	September 2008	Partially completed	<ul style="list-style-type: none"> Policies and processes for accounting for obligations not yet finalized. 	<p><i>Accounting for obligations has an impact on most IPSAS Standards. Appropriate policies are being developed as each Standard is addressed. For example, in the area of PPE, IPSAS compliant process flows to capture goods receipting and invoice matching has been developed. Policies for accounting for obligations can only be finalized with the completion of testing of all relevant processes.</i></p>

Activity	Target Date	Present Status as of 16 th Feb 2009	Activities behind schedule	Management Response
			<ul style="list-style-type: none"> General Policy Document on employee benefits has not been finalized as yet 	<p><i>In the area of Employee Benefits, a full analysis has been conducted of all entitlements of all categories of staff, including the computation method and current process of recording the entitlements. UNIDO specific policies on employee benefits, including policies on accrued annual leave, repatriation grants, after service health insurance (ASHI) have been developed and reviewed by the Sub-Working Group. After receiving feedback from consultants on the point of recognition of three issues (assignment grant, initial shipment and annual leave) end of February 2009, the general policy document has since been drawn up.</i></p>
			<ul style="list-style-type: none"> Employee benefit process flows not finalized 	<p><i>Review of the current processes/systems and recommendation of the necessary changes in business processes and practices is underway.</i></p>
			<ul style="list-style-type: none"> Policy/Accounting for support cost income not finalized 	<p><i>Support cost income has been recognized as being non-exchange revenue during the revenue recognition review. The transfer of associated cash funds is an internal decision and is not directly related to IPSAS.</i></p>
Accounting and reporting to donors	September 2008	Completed	<ul style="list-style-type: none"> The task is considered to be completed as there will be no change in the reporting pattern to the donors. 	
Changes to the Financial System	September 2008	Partially completed	<ul style="list-style-type: none"> AGRESSO upgrade (version 5.5) has not yet been implemented. 	<p><i>While the Agresso upgrade (version 5.5) has not yet been fully implemented, it is currently ongoing.</i></p>

Activity	Target Date	Present Status as of 16 th Feb 2009	Activities behind schedule	Management Response
			<ul style="list-style-type: none"> • Changes have not yet taken effect. • Impact of FPCS and system changes not yet carried out 	<p><i>The Agresso upgrade (version 5.5) is currently ongoing. As mentioned earlier, when the preliminary work programme was drafted for presentation in document IDB.33/5–PBC. 23/5, the assumption was that IPSAS implementation would take place on the then currently available 5.4 version of Agresso. The timelines of the Agresso system upgrade has consequently required adjustment of the timelines of development of system changes and testing. Meanwhile, appropriate system changes and process flows are being developed with the analysis of each key IPSAS Standards, such as PPE, Revenue Recognition, etc.</i></p>
			<ul style="list-style-type: none"> • FPCS inventory module not yet finalized. 	<p><i>Refer to the subsection on PPE above.</i></p>
Testing new business processes in the financial system	December 2008	Partially completed	<ul style="list-style-type: none"> • Exercise on new business processes not yet completed. • Testing in the new system not done because of the delay in AGRESSO upgrade. 	<p><i>For Finance’s comments, please refer to the subsection above on Changes to the Financial System.</i></p>
Review of Financial Regulations	December 2008	Partially completed	<ul style="list-style-type: none"> • Final identification of Financial Regulations that require change has not yet been completed 	<p><i>Work is in progress for harmonization of the Financial Regulations and Rules for the UN system organizations. The main aim of this harmonization initiative is to provide common, simpler and more flexible regulations and rules. Considering this initiative for the UN system, an initial interim review of UNIDO’s Financial Regulations has taken place and only those Regulations that would require to be amended for IPSAS compliance have been identified at this stage. A document is being submitted to the PBC session in early May.</i></p>

Activity	Target Date	Present Status as of 16 th Feb 2009	Activities behind schedule	Management Response
			<ul style="list-style-type: none"> No regulation changed in 2008 	<i>It is inappropriate to change the regulations, when they are still in force under the current accounting framework until 31 December 2009.</i>
Year-end test run for 2008	December 2008	Not done	<ul style="list-style-type: none"> Test run not carried out because of delay in acquisition of upgraded version of Agresso and in other critical areas mentioned above 	

FOLLOW-UP OF THE RECOMMENDATIONS MADE IN PREVIOUS EXTERNAL AUDIT REPORTS
(External Audit Report for the Fiscal Period 2006-07)

S. No.	Recommendation	PBC.24/3 reference	Secretariat's Comments	Auditor's Comments
1	<p>Internal Control Framework:</p> <p>The management committed to examine the Internal Control Framework during 2008-2009 within the ambit of enterprise risk management.</p>	9	<p>Management has already taken some initiatives, through the action plans drawn by the OCC (Operation Coordination Committee), as well as the BPR (Business Process Reengineering) initiative launched by the Director-General.</p> <p>Permanent missions and a number of UN-system organizations were invited by DG to attend a briefing in November 2008 regarding the potential operational efficiencies to be achieved by UNIDO through the implementation of an ERP system and BPR.</p> <p>Subsequent to this presentation, a working group has been set up to explore key dimensions of the change management and to carry forward further work on rationalizing internal processes.</p>	<p>The management has established two forums i.e. OCC and a working group to identify and oversee the BPR requirements.</p> <p>After review of the Action Plans of the OCC and the Working Group, it is recommended that the management may consider aligning the work of these groups with Enterprise Risk Management and developing a time bound plan for institutionalizing the required changes.</p> <p><i>Management's Response:</i></p> <p><i>End of March is the date for finalizing the proposal on streamlining the project cycle, in line with GEF Standards B.1 and B.3, for submission to the EB. If finalizing the process means a decision by the EB, this will be done later than the end of March.</i></p>

S. No.	Recommendation	PBC.24/3 reference	Secretariat's Comments	Auditor's Comments
2	<p>Internal Control Framework:</p> <p>Requirements of the Global Environment Facility fiduciary standards on monitoring of projects-at-risk had been reviewed, with the gap analysis for the monitoring of projects during the project cycle already executed. Further work to carry this initiative forward was expected in 2008, with reference to enterprise risk management.</p>	9(c)	<p>In view of its close linkage with, and major implications for, project management, the issue of projects-at-risk (which is a requirement of <i>GEF Fiduciary Standard B.3</i>) has been dealt with as part of the overall review of UNIDO's technical cooperation cycle that was launched in the 2nd half of 2008, aimed at strengthening the appraisal & monitoring functions and introducing a harmonized quality assurance system, from "<i>quality at entry</i>" to "<i>quality at delivery</i>".</p> <p>One of the tasks of the Inter-branch Working Group, set up to review existing processes and propose a streamlined programme & project cycle, has been the definition of parameters for identifying and monitoring risks within the framework of UNIDO technical cooperation activities, based on the ERM (<i>Enterprise Risk Management</i>) approach.</p> <p>To this effect, the experience of other UN entities (including the World Bank) that are already implementing ERM or related risk management systems has been analyzed and potential measures that appear suitable for adoption by UNIDO have been identified.</p> <p>Major categories of risks (i.e. institutional, financial, administrative and technical) have been defined for the main types of projects undertaken by UNIDO (e.g. institution building, enterprise assistance, meetings/workshops, training, global forum) and recommendations for</p>	Final outcome of review of the working group will be submitted to the Executive Board for approval. The management hopes to finalize the process by the end of March 2009. Significant work has been finalized by the management.

S. No.	Recommendation	PBC.24/3 reference	Secretariat's Comments	Auditor's Comments
			<p>appropriate risk monitoring mechanisms/tools at various stages of the project cycle are being finalized.</p> <p>The overall proposal for streamlining the UNIDO TC cycle and strengthening the quality assurance system (including the risk monitoring part) is to be submitted for review and approval by the Executive Board in February.</p>	
3	<p>Internal Control Framework:</p> <p>The programme development and technical cooperation division was in the process of further clarifying the managerial and administrative responsibilities of its middle management, such as directors and unit chiefs, so that the necessary accountability could be established at an appropriate level within the division.</p>	9(c)	PTC is currently exploring an annual workplan development system that each Branch and Unit can develop, monitor and report its various activity plans in the standardized online format, where directors and unit chiefs are responsible and accountable for necessary actions.	The matter will remain under review of the external audit.
4	<p>Internal Control Framework:</p> <p>The terms of reference for unit chiefs were about to be issued by the human resource management branch, which should also assist in defining clear responsibilities of unit chiefs in the future.</p>	9(c)	HRM has issued the ToRs for unit chiefs in PTC and PSM. The ToRs define the duties and responsibilities of unit chiefs.	<p>The Audit Team verified that ToRs for two divisions have been issued and clearance of draft ToRs for nine unit chiefs is awaited from the PCF Division since long.</p> <p>HRM Branch may continue following up the matter with the concerned division for early clearance of ToRs.</p>

S. No.	Recommendation	PBC.24/3 reference	Secretariat's Comments	Auditor's Comments
5	<p>Internal Control Framework:</p> <p>The possibility to implement e-filing for expenditure incurred through "imprest" accounts would be explored first for "imprest" accounts and later extended to field inter-office vouchers, if possible.</p>	9(d)	<p>There is a facility in the current version of Agresso 5.4 to store documents on imprest transactions that needs to be activated. In the Agresso 5.5 there is an extended document management system that can be also utilized. Upon completion of the update to 5.5, expected in May this year, however, more time needs to be allocated by ICM to actually work on the implementation of the document management system for both imprest and field IOV's.</p>	<p>As intimated by the ICM during discussion the target date for "going live" of Agresso 5.5 is 1st May 2009. The functionality is expected to be put to use thereafter.</p> <p>In the meanwhile management may need to prepare a training plan as well as training material for on-line training of staff at Head Quarters and field offices.</p>
6	<p>Internal Control Framework:</p> <p>As regards performance assessments at the level of projects, management concurred that managerial and administrative matters could be treated in some more depth when performing project reviews and undertook to assign it increased significance.</p>	9(g)	<p>According the UNIDO Evaluation Policy, UNIDO independent evaluations (managed by the Evaluation Group) adhere to UN standards and use the OECD/DAC Evaluation Criteria; Relevance, Efficiency, Effectiveness, Sustainability and Impact. As such they differ from audits and are not done for the purpose of management control. At the same time evaluations are done for the purpose of accountability, enhanced performance and learning and management issues are incorporated in the evaluations when this is found to be relevant. This has for instance been the case in the evaluations of the ITPOs in Italy and France, the COMPID evaluation, the China POPs evaluation and the evaluation of the UNIDO/UNDP Cooperation Agreement.</p> <p>However, in line with the Results Based Management Agenda, UNIDO would like to keep the present focus on the results of the entity under evaluation.</p>	<p>The matter will be taken up in subsequent audits.</p>

S. No.	Recommendation	PBC.24/3 reference	Secretariat's Comments	Auditor's Comments
7	<p>Internal Control Framework:</p> <p>Management also drew attention to the recent establishment of a working group by the UNIDO joint advisory committee that would align the existing individual performance appraisal system to reflect better RBM principles and would harmonize practices in the divisions so that individual performance objectives were clearly formulated based on divisional and branch performance objectives. Team work would also be addressed in this context.</p>	9(g)	<p>A reconstituted group of the JAC is working on this issue and reports periodically to the JAC. Further development on this subject will depend on the availability of resources as well as adequate IT capabilities.</p>	<p>Will remain under review of the External Audit.</p>
8	<p>NON-EXPENDABLE PROPERTY:</p> <p>Inventory records are still not systematically reconciled to the accounting system to ensure its completeness and accuracy.</p>	16	<p>Fixed asset module is currently being used as a stand-alone system without integration to the accounting system.</p> <p>ICM can provide reconciliation reports showing obligations and disbursements which can then be verified and used to update the current fixed asset system periodically.</p> <p>PSM/OSS in cooperation with PSM/FIN and PSM/ICM continues its work on systematic manual reconciliation of the inventory records.</p> <p>PSM/OSS/GES, PSM/FIN and ICM continue to develop and implement reconciliation mechanism of the inventory and accounting records using the functionalities of the recent AGRESSO update. This work is a part of UNIDO's effort related to introduction of IPSAS.</p>	<p>As intimated by the management during discussion, the target date for "going live" of AGRESSO 5.5 is 1st may 2009. The functionality is expected to be put to use thereafter.</p> <p>In the meanwhile management may prepare training plan and training material for on-line training of staff at HQrs and field.</p>

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			With the integration of Agresso 5.5 fixed asset and GL modules, property value will be automatically added to the new fixed system from the accounting transaction. This will eliminate the need for manual reconciliation.	
9	<p>NON-EXPENDABLE PROPERTY:</p> <p>Operational support services branch, in cooperation with the financial services branch and the information and communication management services, would continue its work on systematic reconciliation of the inventory records to the accounting system through further integration of the AGRESSO accounts and fixed asset modules.</p>	17	As explained above on Item 8, the integration of the Agresso fixed assets and GL modules are envisaged in IPSAS implementation.	Same remarks as above in point No. 8
10	<p>RBM data collection system:</p> <p>A methodology for impact evaluation that was tailored towards UNIDO themes and delivery modes was under development.</p>	28	<p>The Results Reporting System (RRS) that was set up and tested in 2007, on a pilot basis, has not been pursued in 2008. As part of the RBM implementation plan a decision was made to analyze the different monitoring instruments and the synergy and consistence of these instruments before rolling out the RRS as UNIDO's RBM data collection system. This analysis is still ongoing.</p> <p>A literature review, covering current trends in impact evaluation was carried out in 2007. UNIDO is carrying out two impact evaluations in 2009; of SMTQ projects in Sri Lanka and of an economic livelihood project (SKIPI) in Uganda. Impact evaluation methodologies will be developed and tested for these two evaluations.</p>	<p>The management is working on developing a methodology for impact evaluation of its programs/projects.</p> <p>The matter will be taken up in subsequent audits.</p>

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			<p>UNIDO is also participating in the development of impact evaluation methodologies and tools through the active participation in international networks; NONIE, UNEG and the Donor Committee on Enterprise Development. Furthermore, UNIDO has initiated a study on "What has UNIDO done to reduce poverty – evidences from UNIDO evaluations" and cooperates with the Global Environment Facility (GEF) on impact evaluation methodologies for environmental projects.</p>	
11	<p>RBM at field offices:</p> <p>Baseline information has yet to be determined to be able to rank field offices' performance according to the categories of those achieving baseline results and those exceeding it or coming in below target.</p>	30	<p>On the occasion of the General Conference, 12th Session, from 3-7 December 2007, UNIDO headquarters organized in Vienna a Result-Based Management training workshop from 10-11 December 2007 for most of the UNIDO Representatives and Heads of Regional Offices and some UNIDO Representatives of Country Offices.</p> <p>The Regional Programmes of the Regional and Field Operations Branch have prepared annual workplans in accordance with RBM principles, and so did the field offices covering nearly all countries. 108 workplans (103 for the field and 5 for the Regional Programmes) have been uploaded on the Intranet in an improved format in Excel.</p> <p>The Asia and the Pacific Programme (ASP) has prepared a consolidated quarterly RBM report and submitted to Management for information based on the reports from field offices from the beginning of 2008. Highlights of Field</p>	<p>The matter will remain under review of the external audit.</p>

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			<p>Office Quarterly Reports against RBM Work Plan were provided for April–June 2008 and for July–September 2008. ASP analyzed the reports from field offices and provided feedback to them.</p> <p>In the Latin America and the Caribbean Programme, the six-monthly reports are pending. The field office yearly reports will be prepared until the end of 2008 but are still pending, apart from one UNIDO Desk. RBM based workplans have been prepared for field offices and regional offices.</p>	
12	<p>Internal Oversight Services:</p> <p>The hotline and reporting tool now require Institutionalization towards achieving effective whistle blowing.</p>	Annex 1	<p>The web-based reporting tool developed between IOS and ICM has been ready for launch since September 2007.</p> <p>Launch has been delayed, awaiting clarification from senior management on separate or joint reporting mechanisms by type of allegations, i.e. fraud/wrongdoing (IOS mandate); sexual/work harassment and abuse of authority (in HRM), retaliation against whistleblower (in the ethics function – placement to be determined), and further on the reporting tool's accessibility: intranet only or also internet (IOS preferred option and compliance with fiduciary standards).</p> <p>Once clarified (expected shortly), IOS, supported by ICM, will proceed with modifications, if any, and launch the tool.</p>	<p>The functionality has been pending for 17 months. The management may like to expedite the critical decisions so that the reporting tool may become operational.</p> <p><i>Management's Response:</i></p> <p><i>Management has made the decisions needed and authorization to IOS to proceed. The tool has been accordingly modified. It is already accessible through the IOS page on the intranet, and through the fraud alert page on the internet. It will be linked to the "main page" of the UNIDO website in the coming days (depending on available resources) and once done, will be announced by email throughout the Organization.</i></p> <p>The matter will remain under review of the External Audit.</p>
13	<p>Internal Oversight Services:</p> <p>In compliance with the Institute of Internal Auditors (IIA) standards, an independent external quality</p>	Annex 1	<p>The external quality assessment of the internal audit activities of IOS has been completed and concluded in November 2008. Following IIA standards and</p>	<p>External quality assessment of Internal Audit verified.</p> <p>External quality assessment of investigative activities, however begs prompt attention</p>

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	assessment of the IOS is required at least once every five years. The external quality assessment now being overdue remains cause for concern.		<p>acceptable methodology, it was conducted as a self-assessment validated by an external body to the organization, i.e. the Institute of Internal Auditors itself. The outcome was shared with senior management.</p> <p>Modalities for similar exercise for investigative activities (also part of IOS mandate) are under discussion at the Conference of Investigators and once finalized, will be considered by IOS.</p>	<p>on account of the fact that it is overdue.</p> <p><i>Management's Response:</i></p> <p><i>The IIA standards, and therefore the 5 year requirement, apply to the internal audit side of IOS.</i></p> <p><i>The investigative activities follow different standards, i.e. the UN system guidelines for investigations (endorsed at the 3rd Conference of International Investigators in 2003, the members being the UN system organizations, the Multilateral Financial Institutions and other public sector organizations). The present guidelines do not include a compulsory external quality assessment. A revised version of the guidelines for investigations is currently under discussion at the Conference of International Investigators, and include a peer review standard. Once the new guidelines are finalized and endorsed (the next Conference is scheduled for June 2009), IOS will consider the matter, learning from the three organizations having or currently undergoing/piloting such peer review. Therefore, an external quality assessment of investigative activities is not overdue.</i></p> <p>The matter will remain under review of the External Audit.</p>
14	<p>Non-expendable property:</p> <p>The management of non-expendable property at the field offices is in need of some improvement. The effect of the manual in improving property management at the field offices is yet</p>	Annex 1	PSM/OSS regularly follows up with the UNIDO Field Offices concerning physical inventories/verification of their records providing them with necessary assistance and emphasizing the importance of the regular physical checks of the assets. In the same context	Quantitative Impact of the knowledge sharing on procurement and inventory management by the field offices is appreciable. Management may, however, conduct a qualitative review of the annual inventories submitted by the field offices.

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	to be assessed.		<p>in order to increase awareness of Field Offices, PSM/OSS provided in 2007 training to the Field staff responsible for property management and prepared all necessary guidelines and reference documentation which are available on the Intranet at http://intranet.unido.org/intra/Inventory_Control and are accessible to all Field Offices staff.</p> <p>It should be noted that in general we witness a positive change in this area. In 2008 all operational Field Offices and UNIDO Desks submitted their verified inventories to PSM/OSS by the end of December 2008. This is already a second consecutive year when the December deadline is met, which proves that the positive trend has become sustainable (It is to be noted that prior to 2007 the inventories were received as late as the end of the first quarter of the following year.)</p> <p>The above notwithstanding, PSM/OSS with support of the senior management, specifically of the Programme Coordination and Field Operation Division (PCF), continues with its efforts aimed at achieving full compliance with the rules and procedures governing UNIDO's property management. To this effect PSM/OSS is in constant contact with PCF to secure their support in ensuring compliance of the Field Offices with the rules and procedures governing assets management, with particular emphasis on regular physical inventories and maintenance of reliable assets</p>	

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			<p>identification (labelling) system. Such compliance must be taken into account in evaluating performance of Field Offices since only through this joint and coordinated effort overall improvement of UNIDO's property management could be achieved.</p> <p>PSM/OSS proposed that PCF and PTC instruct newly appointed staff to consult PSM/OSS/GES directly for training on property management. Emphasis shall be placed on self-training for Field Office and Technical Cooperation staff using the reference documents and presentations available on the Intranet on PSM/OSS/GES page.</p> <p>Upon request of the Director, PSM/OSS, in an e-mail dated 22 May 2008 RFO/OD advised all Heads of Regional Offices, UNIDO Representatives and Heads of UNIDO Operations to ensure compliance with the rules of UNIDO Field Offices property management, in particular the provisions of the UNIDO Property Management Manual, which is available on the Inventory Control site of the UNIDO Intranet together with a related PowerPoint presentation on Property Management at UNIDO field Offices.</p>	
15	<p>Procurement:</p> <p>Procurement plans were incomplete and the organization could enhance their use as management and monitoring tools. Procurement plans were finalized. However, difficulty was still experienced in collecting the</p>	Annex 1	<p>Inputs for the procurement plan had been provided by project managers of the PTC Division as part of its annual workplan development in 2008. The practice continues in 2009. Feedback from the procurement service on the plan and further communication between relevant personnel is required for it to be an</p>	<p>Although positive developments have been initiated, the benefits of effective procurement management are yet to be fully realized.</p> <p>The matter will remain under review of the external audit.</p>

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	<p>necessary inputs from all users in order to use these plans effectively as a management and monitoring tool. The benefits from effective management and monitoring of procurement are yet to be realized.</p>		<p>effective management and monitoring tool.</p> <p>PTC in cooperation with PSM/OSS has started to apply Intranet Procurement Planning Module to monitor UNIDO TC delivery since 2007. The monitoring involves preparation of the annual procurement plan/forecast by PTC and regular meetings of procurement and requisitioning staff to discuss its implementation. The detailed procurement planning procedure was introduced through issuance of the UNIDO Procurement Manual in February 2008. The above measures have positively reflected on the TC implementation in 2008 and allowed to avoid last minute requisitioning. However, procurement planning has not yet become a must and further effort on behalf of PTC is required. This was reflected in OCC Matrix of October 2008 submitted for approval of the DG. The improvement in procurement planning shall be accompanied by further computerization of the process using the expanded functionalities of the recent AGRESSO update.</p> <p>Online training on procurement commenced in 2008 and a more advanced training will be implemented in 2009.</p> <p>PCF staff members, including field staff, involved in procurement have been requested to do the procurement self-study/self-training based on the Procurement Manual, which explains the</p>	

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			information necessary from Allotment Holders for the preparation of the Procurement Plan, and to do the online procurement test. A special communication from HRM/OSS/PRS to Allotment Holders emphasizing the importance of providing inputs to the Procurement Plan may be considered, in order to improve the collection of inputs.	
16	<p>Environmental policy and management strategy:</p> <p>UNIDO has not developed and implemented a formal environmental policy and management strategy. The matter remains under review until such time as the organization formally develops and implements a comprehensive environmental policy and management strategy.</p>	Annex 1	<p>Although UNIDO has not yet developed a comprehensive environmental policy and management strategy, it is acutely conscious of environmental and climate-related issues, not least because of its extensive technical cooperation activities in the field and the appointment of the Director-General as Chair of UN Energy. The Organization has therefore taken a number of steps to reduce the environmental impact of its operations, inter alia by establishing a strategy to reduce its carbon footprint and by introducing measures to enhance environmental awareness in the context of its procurement activities. UNIDO fully accepts the recommendations of the external auditors with regard to the need to formulate and adopt a comprehensive environmental policy and management strategy, however, and intends to launch an initiative to this end in the near future. (OSL/OCC)</p>	<p>The management is fully aware of the need to devise a comprehensive environmental policy and intends to launch an initiative in this direction.</p> <p>The matter will remain under review of the external audit.</p>

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17	<p>End-of-service and after-service health insurance liabilities:</p> <p>Budgetary provision has not been made to cover the estimated costs of contingent liabilities for end-of-service payments to staff. Similarly, liabilities in respect of after-service health insurance have not been fully funded. The matter remains under review. No progress has been made.</p>	Annex 1	<p>With the decision to adopt IPSAS in the UN System organizations, End-of-service benefits and ASHI liabilities has become a more critical issue. The United Nations as the lead agency on this issue is in the process of obtaining some guidance from the General Assembly.</p> <p>The actuarial study on UNIDO's ASHI liabilities was concluded and the results were disclosed in the Biennium 2006-2007 financial statements.</p> <p>As part of IPSAS implementation by Jan. 2010, a working group involving various branches has been looking into practical steps to be fully IPSAS compliant regarding EOS and ASHI benefits in terms of recognizing the related liability.</p>	<p>The matter will remain under review of the external audit.</p>