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REPORT OF THE UNITED NATIONS BOARD OF AUDITORS ON THE
FINANCIAL STATEMENTS OF THE VOLUNTARY FUNDS ADMINISTERED BY
THE UNITED NATIONS HIGH COMMISSIONER FOR REFUGEES
FOR THE YEAR ENDED 31 DECEMBER 2001^{*/}

^{*/} An annex contains follow-up actions by the Administration to implement the Boards' recommendations for 2000, as well as the comments of the Board.

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CHAPTER I

FINANCIAL REPORT FOR THE YEAR ENDED 31 DECEMBER 2001

A. Operations

1. Providing international protection to refugees and other persons of concern, and seeking permanent solutions to their problems are the primary functions of the Office of the United Nations High Commissioner for Refugees (UNHCR). UNHCR efforts are mandated by the organization's statute, and guided by the 1951 United Nations Convention relating to the Status of Refugees and its 1967 Protocol. International refugee law provides an essential framework of principles for the Office's humanitarian activities. The activities of the Office, defined as non-political, humanitarian and social, have been further reinforced and guided by subsequent General Assembly resolutions, as well as conclusions and decisions of the Executive Committee of the High Commissioner's Programme. They are carried out within a framework comprising refugee, human rights and humanitarian laws, and internationally accepted standards for the treatment of refugees and other persons of concern to UNHCR.
2. The primary purpose of UNHCR is to safeguard the rights and well-being of refugees. In its efforts to achieve this objective, UNHCR strives to ensure that everyone can exercise the right to seek asylum and find safe refuge in another State, and to return home voluntarily. By assisting refugees to return to their own country or to settle permanently in another country, UNHCR also seeks lasting solutions to their plight. In support of its core activities on behalf of refugees, the Executive Committee of UNHCR and the General Assembly have authorized the organization's involvement with other groups. These include former refugees who have returned to their homeland; internally displaced persons; and people who are stateless or whose nationality is disputed.
3. In 2000, the fiftieth anniversary of the creation of UNHCR was followed by celebrations of 50 years of the 1951 Convention relating to the Status of Refugees. Although drafted and signed in a very different geopolitical context, this instrument, together with its 1967 Protocol, has been and remains the steadfast bedrock of the international refugee protection regime.
4. The Global Consultations on International Protection, launched late in 2000, gave rise in 2001 to a series of events, of which the most important was the Ministerial Meeting of States Parties to the 1951 Convention and/or its 1967 Protocol, held in Geneva in December 2001. The Global Consultations has proved to be a unique process that has involved representatives of States from all regions, intergovernmental and non-governmental organizations, academics and refugees. The process gave UNHCR renewed impetus to pursue its efforts to ensure that refugees and asylum-seekers alike enjoy the international protection that they deserve. It is scheduled to conclude shortly and will result in an agenda for protection for the years to come.
5. Persistent instability and strife have continued to cause population movements particularly in countries of Africa and parts of South America, but there were no major refugee emergencies comparable to the scale of those that occurred in the 1990s. The emergency response capacity of UNHCR was

nevertheless primed on several occasions in the course of the year, notably in West Africa early in 2001, South-East Europe in the summer, with prospects of major movements from the former Yugoslav Republic of Macedonia, and in countries bordering Afghanistan in the autumn. In most of these cases, interventions at a political level caused events to take another course and the threat of large-scale outflows was generally averted.

6. In 2001, UNHCR cared for an estimated 19.8 million asylum-seekers, refugees and others of concern to the Office in almost 160 countries. The region of South-West Asia hosted the largest refugee population (40 per cent), followed by Africa (26 per cent) and Europe (17 per cent). The largest groups of prima facie refugee arrivals in 2001 were: Afghans arriving in Pakistan (200,000); refugees from the former Yugoslav Republic of Macedonia, who entered the Federal Republic of Yugoslavia; and refugees from the Central African Republic who sought asylum in the Democratic Republic of the Congo.

7. During the past year, UNHCR recorded a number of achievements in several regions. In Africa, some of these included the repatriation of some 100,000 Sierra Leonean refugees from the neighbouring countries. UNHCR alone, cannot take all the credit for this. The successful completion of the disarmament process by the United Nations Mission in Sierra Leone, coupled with the Government's official declaration of the end of the war and impending presidential elections all contributed to the stability in the country. In Eritrea, after many years in exile, some 36,000 refugees returned to their homes from the Sudan. Another successful repatriation was the return of over 50,000 refugees from Ethiopia to north-west and north-east Somalia. In the Great Lakes region of Africa, although many of the conflicts have not yet been resolved, there were some positive developments in 2001. Nearly 30,000 refugees returned to the northern provinces of Burundi, where the security situation was relatively good. In the Democratic Republic of the Congo, with the deployment of the United Nations Organization Mission in the Democratic Republic of the Congo, this played a crucial role in separating armed combatants who fled from the Central African Republic to the Democratic Republic of the Congo, together with over 24,000 refugees. There has also been some success in Europe. In the Balkans, over two million people who were forced to flee their homes during the last 10 years of war have returned home. In southern Serbia, UNHCR played a role in preventing new violence by promoting measures such as the creation of a multi-ethnic police force. In the former Yugoslav Republic of Macedonia, UNHCR in consultation with the European monitors and the North Atlantic Treaty Organization was instrumental in rebuilding confidence between communities and assisting more than 80 per cent of the 170,000 people who were displaced last year to return to their homes. Similarly, in Bosnia and Herzegovina and Croatia, some 100,000 refugees and internally displaced persons have been able to go home. However, significant challenges remain. There are still over 800,000 people from those countries who have not been able to return to their former homes. UNHCR is continuing in its efforts to ensure that local authorities implement property laws and assist with reconstruction of properties destroyed by the war. In Asia, almost 193,000 East Timorese were successfully repatriated from West Timor. On another positive note, and a successful example of local integration in 2001, the Government of Mexico naturalized more than 1,300 Guatemalan refugees who chose not to repatriate. In addition, the government of Quintana Roo State donated a substantial amount of land for

these former refugees to ensure the sustainability of their local integration. In 2001, UNHCR facilitated the resettlement of some 33,400 refugees from 75 first asylum countries to 23 countries of permanent residence.

8. Throughout 2001 and early 2002, both in areas concerning protection and assistance activities and in its general management of the Office's resources and presence across the world, UNHCR paid particular attention to a number of important cross-cutting themes. Many of these themes provided opportunities for strengthening both internal and external partnerships in order to coordinate appropriate, cost-effective and timely responses. The most notable recent example was the launching of the inter-agency response to reconstruction efforts in Afghanistan, where consideration of environmental issues and the development of sustainable solutions for self-reliance in newly returned communities will be crucial. Across the globe, but perhaps most acutely in Africa, the urgent need to develop HIV/AIDS awareness and integrate proactive measures into its protection and assistance role is of high priority for UNHCR.

B. Budget and expenditure for 2001

9. Severe funding constraints already experienced in recent years again affected UNHCR's activities in 2001. An initial target of \$898.5 million was approved by the Executive Committee in October 2000, at its fifty-first session. During the course of 2001, seven supplementary programmes, with a total value of \$117 million, were approved, notably for operations in Afghanistan, Eritrea, Sierra Leone and for needs resulting from the situation in the former Yugoslav Republic of Macedonia, taking the total to \$1,015.5 million. However, total income throughout the year fell considerably short of requirements. This inevitably led to budget cuts and measures to manage the shortfall in the course of the year, which affected many operations.

10. Within the confining limits of available resources, expenditure for the year totalled some \$801 million. It reveals that expenditure was highest in Africa (some \$307 million), followed by South-East Europe (\$112 million) and South-West Asia, Central Asia and the Middle East (\$105 million). In terms of types of assistance, the largest share was for care and maintenance pending durable solutions (some 32 per cent of total expenditure), again mainly in Africa. Expenditure on voluntary repatriation, local settlement and resettlement (the three durable solutions) accounted for 28 per cent of total expenditure.

11. It was this context of financial shortfalls that prompted the introduction of "Actions 1, 2 and 3". This involved a thorough review of all operations, based on a careful analysis of what could be considered "core" and "non-core" activities, leading to budget and staff reductions as field offices were closed in some areas. For its part, the Executive Committee also held a series of consultations on budget issues during the year in an attempt to help find solutions.

12. As part of these efforts to increase and ensure more stability of its income, UNHCR has continued to work towards obtaining a larger contribution from the United Nations regular budget. Over the years, this contribution has

dwindled to a minimal percentage of requirements. With the support of the Advisory Committee on Administrative and Budgetary Questions, a commitment to a modest increase was obtained for the biennium 2002-2003, but the regular budget contribution still falls far short of the full amount to which the Office should be entitled as envisaged under its statute.

13. The year 2001 also witnessed the beginning of a new strategy to increase funds raised from the private and corporate sector through a network of staff and national associations at work in 15 countries. Over \$20 million were raised in the course of the year, the largest amounts being in Italy, the United States of America and Japan, with Spain and Germany close behind. The Executive Committee featured a panel discussion on "broadening support to refugees" at its fifty-second session, to help raise awareness of the potential partnership between humanitarian work and the corporate world and civil society. For durable results, however, a consistent effort will be required, which in turn demands an investment of resources by the Office.

C. Financial results

14. The UNHCR voluntary funds balance (without the United Nations regular budget line of \$20.4 million) as at 1 January 2001 was \$128.4 million. This, together with the voluntary contributions of \$779.2 million, interest income of \$4.7 million, miscellaneous income of \$4.8 million, cancellation of prior years' obligations of \$20 million, and taking into account the currency exchange losses of \$14 million and prior years' adjustments of \$8.4 million, resulted in funds available totalling \$931.5 million. Expenditures amounted to \$782.6 million. After taking into account the above, the fund balance as at 31 December 2001 reflected a net surplus of \$148.9 million, which are carried forward to the year 2002.

15. Statement I shows the income, expenditure and the changes in reserve and fund balances of the voluntary funds administered by UNHCR. Statement II shows UNHCR assets, liabilities, reserves and fund balances for the voluntary funds.

16. Statement III shows the cash flow for the voluntary funds administered by UNHCR for the year ended 31 December 2001, and that UNHCR had \$140.5 million cash and term deposits at the end of the year 2001.

CHAPTER II

REPORT OF THE BOARD OF AUDITORS

Summary

The Board of Auditors has audited the financial statements of the voluntary funds administered by the United Nations High Commissioner for Refugees for the period from 1 January to 31 December 2001. The Board has also reviewed the operations of the voluntary funds administered by the High Commissioner at the headquarters of the Office of the United Nations High Commissioner for Refugees (UNHCR) in Geneva and at offices in Bosnia and Herzegovina, the Democratic Republic of the Congo and the United Republic of Tanzania for the same period.

The Board's main findings are as follows:

(a) The unliquidated obligations reported in the financial statements (\$74 million) are not recorded in the UNHCR general ledger, but are equal to the difference between spending authorizations and disbursement; as a consequence, in this regard, the financial statements present only an estimation of the UNHCR expenditure for the year, instead of reflecting the actual expenditure;

(b) From June 2001 to June 2002, UNHCR succeeded in reducing by \$43.9 million the expenditure not yet justified by implementing partners' financial reports; as at 21 June 2002 a total expenditure of \$4.3 million relating to the years from 1994 to 2000, and \$7.5 million relating to 2001, remained without such financial reports;

(c) One country has continued to deny UNHCR access to accounting records of implementing partners with expenditures totalling \$4.1 million in 2001;

(d) Within the \$204.7 million 2000 expenditure covered by audit certificates received at the end of March 2002, the Board reviewed \$124 million and found that audit certificates for \$106 million (86 per cent) lacked reference to the implementing partner financial report, of which \$91.5 million pertained to implementing partners not required to present them under UNHCR rules. Another \$27.6 million had no clear certification that funds had been used in accordance with the project agreements;

(e) As an overall result, UNHCR has insufficient assurance that the funds are properly used, even after enough time has elapsed for submission of the certificates;

(f) Contrary to the UNHCR statute, the United Nations regular budget does not fund most of UNHCR administrative expenditure: in 2001 it funded only 37 per cent of the management and administration costs, or 8 per cent, when including programme support costs;

(g) Available reserves at the end of 2001 (\$92.4 million) were, as in other United Nations entities, far from being sufficient to cover the staff termination liabilities estimated at some \$228 million;

(h) Pledges for contributions made in currencies other than the United States dollar are recorded at the United Nations exchange rate at the time of recording the pledge, but UNHCR does not hedge against the related exchange rate risks; as a consequence, currency exchange losses on pledges recorded in the 2001 financial statements amounted to \$12.4 million;

(i) The current UNHCR information system, which is different from the United Nations core Integrated Management Information System (IMIS), is not an integrated system. The configuration and the number of applications leave it open to a considerable risk of errors. Because of an expected change to a new system, there have been few upgrades, and the gap between the current system and functional requirements has widened;

(j) The introduction of a new system, however, has been delayed. In June 2001, UNHCR put a new Integrated System Project on hold, considering rightfully that it failed to comply with best practices for project management, as highlighted by the Board in its last report. As of May 2002, a final decision was still pending, but expenditure on the project had already amounted to some \$13 million – 38 per cent of the initial budget – with no operational result.

While acknowledging the valuable progress made by UNHCR in monitoring its implementing partners, the Board made recommendations, principally to improve the accounting for expenditure, the audit certificate procedures, the cash management, and the reliability of the information systems. It has noted that, in most respects, UNHCR has actively responded to recommendations, although some have yet to be implemented.

A list of the Board's main recommendations is contained in paragraph 13 of the present report.

A. Introduction

1. In accordance with paragraph 22 of the statute of the Office of the United Nations High Commissioner for Refugees (UNHCR), the Board of Auditors has audited the financial statements of the voluntary funds administered by the High Commissioner for the period from 1 January to 31 December 2001.

2. The audit was conducted in accordance with article XII of the Financial Regulations of the United Nations and the annex thereto and with the common auditing standards adopted by the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency. Those auditing standards require that the Board plan and perform the audit to obtain reasonable assurance that the financial statements are free of material misstatement.

3. The audit was conducted primarily to enable the Board to form an opinion as to whether the expenditures recorded in the financial statements for the period from 1 January to 31 December 2001 had been incurred for the purposes approved by the Executive Committee of UNHCR; whether income and expenditures were properly classified and recorded in accordance with the Financial Regulations and Rules; and whether the financial statements of the voluntary funds administered by the High Commissioner for Refugees presented fairly the financial position as at 31 December 2001. The audit included a general review

of financial systems and internal controls and a test examination of the accounting records and other supporting evidence to the extent the Board considered necessary to form an opinion on the financial statements.

4. The audit was carried out at UNHCR headquarters in Geneva and at its offices in Bosnia and Herzegovina, the Democratic Republic of the Congo and the United Republic of Tanzania.

5. In addition to the audit of the accounts and financial transactions, the Board carried out reviews under article 12.5 of the Financial Regulations of the United Nations. In 2001, the Board reviewed, in particular, cash management and the financial information systems.

6. The Board continued its practice of reporting the results of specific audits through management letters containing audit findings and recommendations to the Administration. The practice allowed an ongoing dialogue with the Administration on issues arising from the audit.

7. The present report covers matters which, in the opinion of the Board, should be brought to the attention of the General Assembly. The Board's observations on all matters contained in the present report were communicated to UNHCR. The Administration confirmed the facts on which the Board's observations and conclusions were based and provided explanations and answers to the Board's queries. The report is divided into two parts, covering the audit of financial issues and management issues, respectively.

8. The Board's main recommendations are reported in paragraph 13 below. The detailed findings are discussed in paragraphs 18 to 101.

1. Previous recommendations not fully implemented

9. In accordance with section A, paragraph 7, of General Assembly resolution 51/225 of 3 April 1997, the Board has highlighted separately below those recommendations that have not been fully implemented.

10. Two major recommendations made by the Board between 1995 and 1999 have yet to be implemented. The Board recommended that the Administration:

(a) Make the preparation of work plans an integral part of the project-planning and monitoring process (1995, 1996, 1998 and 1999);

(b) Ensure complete and accurate disclosure of non-expendable property and conduct physical stock checks on a regular basis (1996, 1997, 1998 and 1999).

11. On the first recommendation, the Board noted that the production of a guide for use of work plans when preparing projects and subprojects has not been finalized within the initially foreseen time frame, as UNHCR has faced staffing and operational problems. However, a first draft of a mini-guide has been circulated for review and comments of staff. With regard to the second recommendation, the Board noted that the value of non-expendable property was still understated in the 2001 financial statements, at \$252.4 million for the acquisition value and \$43.5 million for the depreciated value. As highlighted in January 2002 by the Office of Internal Oversight Services (OIOS), some

1,500 headquarters items were not recorded, assets in the custody of implementing partners were not fully accounted for and some 4,000 items were recorded at a default value, understating the current value by some \$4.8 million. The last physical inventory of headquarters assets was started in 1999 but never completed. UNHCR is committed to reducing the default values in its asset management system to its minimum by the end of 2002. The Board encourages UNHCR to improve the overall situation.

12. In accordance with General Assembly resolution 48/216 B of 23 December 1993, the Board also reviewed the measures taken by the Administration to implement the recommendations made by the Board in its report for the year ended 31 December 2000.¹ Details of action taken and the comments of the Board are outlined in the annex to the present report.

2. Main recommendations

13. The Board recommends that UNHCR:

United Nations system accounting standards

(a) **Modify its accounting policy and financial system on expenditure in order to comply with United Nations system accounting standards through an accurate accounting of disbursements and valid unliquidated obligations (para. 38);**

Implementing partner expenditure

(b) **Assess the feasibility and cost-effectiveness of modifying the rules on the control of implementing partners expenditure, with a view to obtaining audit certificates covering the financial reports submitted by the international non-governmental organizations and governmental partners; monitor corrective action taken by field offices in case of audit certificates with qualification or major findings and document the follow-up; consider the establishment of a comprehensive database on local audit resources history and results to facilitate audit monitoring and risk assessment (paras. 63 and 73);**

Cash management

(c) **Manage exchange rate risks by adopting a more proactive, hedging stance (para. 78);**

(d) **Set and regularly update a comprehensive database in respect of bank services, based on written agreements, and launch a competitive bidding for all headquarters bank accounts, in order to obtain the best condition and services (para. 80);**

Information systems

(e) **Address the current functionality deficiencies and define a clear development strategy needs for its Financial Management Information System**

¹ Official Records of the General Assembly, Fifty-sixth Session, Supplement No. 5E (A/56/5/Add.5).

(FMIS), factoring in the technological delays that have built up with FMIS developments over the last few years, and the decisions that will be taken to restart the Integrated System Project or a similar project and its provisional roll-out date. The Board further recommends that, as long as FMIS produces the accounts, a risk-estimation procedure be implemented (para. 88);

(f) Consult with the United Nations Secretariat and other relevant United Nations entities to ensure that in terms of cost-benefit the present diversity of information systems approaches is in the best interest of Member States and of the beneficiaries of United Nations programmes; ascertain that there are no ready-made solutions, even at the cost of alterations in current UNHCR procedures, preferably within the United Nations system (para. 100).

14. The Board's other recommendations are presented in paragraphs 21, 29, 31, 41, 53, 56, 66, 68, 71, 82, 84, 90, 94.

3. Follow-up on special requests from the
General Assembly and the Advisory Committee on
Administrative and Budgetary Questions

15. The General Assembly, in its resolution 56/233 of 24 December 2001, reiterated its position that a biennial audit would give UNHCR more time to implement the recommendations of the Board and would also facilitate the timely submission of audit certificates by implementing partners. UNHCR has indicated that it "is not planning to move to a biennium cycle, the main reason for that position being the specific nature of UNHCR's work and its related planning and funding aspects".

16. While noting the UNHCR position, the Board has examined with UNHCR the legal and technical elements of the issue, in order to provide further data to the General Assembly, and concludes that:

(a) Changes towards a biennial audit would require minor legal modifications in the UNHCR statute and Financial Rules. The General Assembly would have to modify the timing pattern of its review of the arrangements for the Office of the High Commissioner. The General Assembly determines periodically whether the Office should be continued: this has been done thus far on a five-year basis, and most recently, for a period extending to 31 December 2003. To ensure consistency between the UNHCR accounts and the biennial reports of the Board, it should be done on the base of a multiple of two years, beginning on 1 January 2004. The Financial Rules of UNHCR, which specify annual audits, would have to be likewise modified;

(b) More materially, such a change would require prior alterations in the UNHCR information system. The Board, mindful of the costs and perils of software customization, considers that it might be costly and inefficient to request UNHCR to modify its present data-processing system, soon to be replaced, but that an estimate of the cost of the adaptation of its next system to a biennial audit cycle would be desirable. The Board also notes that, if the cost is limited, such an eventuality should be provided for;

(c) A biennial audit would be consistent with the overall United Nations audit cycle. However, the uniqueness of UNHCR, such as its management and reporting cycle, have to be taken into account.

17. The Board recommends that (a) should the General Assembly wish to pursue the matter, it should request UNHCR to perform a detailed review and cost-estimate of the modifications implied by a biennial cycle; and that (b) regardless of the outcome, UNHCR examine the cost of taking into account in its new information system the possibility of biennial cycles.

B. Financial issues

1. Financial position

18. The UNHCR financial statements relate to the voluntary funds administered by the High Commissioner for the period from 1 January to 31 December 2001. Apart from these voluntary funds, UNHCR receives funding from the United Nations regular budget. The related assessed contributions are disclosed for information in schedule 1 to the UNHCR financial statements and are reported in the United Nations General Fund financial statements (vol. I).

19. UNHCR relies almost entirely on income from voluntary contributions, which amounted to \$779 million in 2001 while regular budget resources totalled \$20 million (2.5 per cent of voluntary contributions). According to the statute, the "administrative expenditure relating to the functioning of the Office of the High Commissioner shall be borne on the budget of the United Nations". "Administrative" is commonly understood as opposed to "operational". It refers to categories of costs as defined in note 5 to the financial statements, and covers therefore either (a) in a restrictive meaning, the "management and administration costs" relating to headquarters, or (b) when construed in a more extensive meaning, "programme support costs", that is, of a technical, logistical or administrative nature, both at headquarters and in field offices.

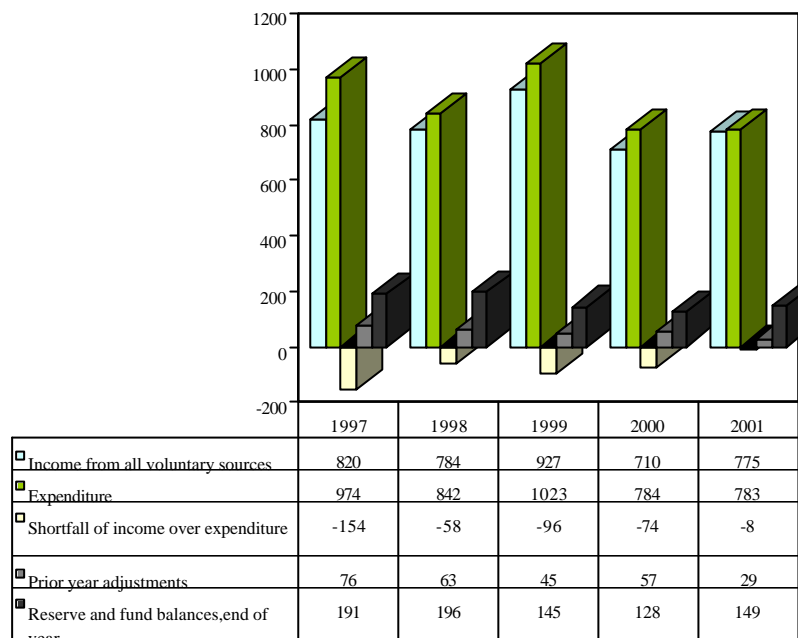
20. Contrary to the UNHCR statute, the United Nations funded in 2001 only 37 per cent of the management and administration costs, or 8 per cent when including programme support costs. In its resolutions 52/220 and 54/249, the General Assembly requested the Secretary-General to review the funding of the Office of the High Commissioner for Refugees from the regular budget above the current proposed level. UNHCR indicated that the United Nations Secretariat had agreed in principle to phased increases over the three coming bienniums, and that the proposal was being discussed by the competent bodies of the General Assembly.

21. The Board recommends that: (a) UNHCR formally state the scope of "administrative expenditure"; and (b) the UNHCR statute be eventually amended should the planned phased increases from the United Nations regular budget not be sufficient to fund UNHCR administrative expenditure.

Overall financial position

22. The following graph and table 1 reflects the financial position over the past five years and the level of reserves compared to the longer-term liabilities disclosed in note 13 to the financial statements.

**Table 1 Financial position 1997-2001
(in millions of United States dollars)**



23. Over the period, income has declined from \$820 million to \$775 million (6 per cent), and expenditure from \$974 million to \$783 million (24 per cent). Although shortfalls of income over expenditure were partly covered by prior year adjustments, UNHCR reserves have been drawn upon to meet shortfalls, and have been reduced from \$191 million to \$149 million (28 per cent) over five years.

24. However, the trend has been reversed in 2001. The shortfall of income over expenditure has been reduced. This is partially owing to the restriction of 2001 expenditure by the new High Commissioner at the level of expected income, notwithstanding the Board's finding on unliquidated obligation accounting as mentioned below. In addition, total reserves increased by \$20 million following an increase of \$42 million in the Supplementary Programme Fund reserves.

25. As regards the liquidity position, UNHCR has maintained its assets to liabilities ratio at 2.4:1, with assets of \$255 million and liabilities of \$106 million (compared with \$217 million of assets and \$89 million of liabilities at the end of 2000).

**Table 2 Liabilities for end-of-service and post retirement benefits
(in millions of United States dollars)**

| | 1999 | 2000 | 2001 |
|--------------------------------|----------------|----------------|----------------|
| After-service health insurance | 230 | 260 | 91 |
| Accrued annual leave | 25-30 | 18-20 | 19-21 |
| Termination benefits | 22-27 | 105 | 116 |
| Total range | 277-287 | 383-385 | 226-228 |

26. Evolution of liabilities for after-service health insurance, accrued annual leave and termination benefits is reflected in table 2, with the spread as indicated by UNHCR.

27. The termination benefits liabilities have increased fivefold between 1999 and 2000. As mentioned in its last report,¹ the Board examined the revised estimates of the liability for termination benefits and considered them to be reasonable.

28. The after-service health insurance liabilities have decreased by a factor of three between 2000 and 2001, after consulting an actuary. The actuarial study was based on 5,046 active staff and 323 retirees as at 1 January 2000, when figures at the end of 2001 would have been more accurate – and would have changed the liability amount (5,208 active staff as at 1 January 2002). There is a significant discrepancy between the number of active staff used for estimating after-service health insurance liabilities (5,046 staff members) and the number used for annual leave and termination benefits estimates (5,881), mostly owing to 700 additional staff members recently recruited in Afghanistan and not yet recorded in the UNHCR personnel database.

29. The Board recommended that UNCHR adopt a consistent policy with regard to the number of staff members to be taken into account for calculation of termination liabilities. UNCHR agreed.

30. Reserves and fund balances held by UNHCR at the end of 2001 amounted to \$148.9 million, out of which \$56.5 million was earmarked for specific purposes (\$12.4 million for the Medical Insurance Plan, \$6.1 million for the Junior Professional Officers Fund and \$38 million for the Working Capital and Guarantee Fund). Available, non-earmarked reserves (\$92.4) are far from being sufficient to cover the staff termination liabilities as estimated in note 12 (some \$228 million as reported above), which is a matter of great concern. UNHCR is aware of the unfunded liabilities, which is a United Nations system-wide problem currently under review.

31. The Board recommends that UNHCR, in conjunction with United Nations Headquarters, review the funding mechanism and targets for end-of-service liabilities in line with other United Nations organizations.

2. United Nations system accounting standards

32. The Board assessed the extent to which the UNHCR financial statements for the year ended 31 December 2001 conformed to the United Nations system accounting standards. Further to the Board's audit, UNHCR has made four major adjustments so that they be generally consistent with the standards. Those adjustments relate to pledges receivable, a transfer from the Junior Professional Fund to the Annual Programme Fund of fees for administrative management (\$2.75 million), a reduction in income of the Medical Insurance Plan (by \$1.36 million), disclosure of ex gratia payments (increased by \$838,391). Assets as at 31 December 2001 have accordingly been reduced from an initial \$257 million to \$255 million and the 2001 Fund balance has been reduced by the same amount. In addition, further to the Board's requests, notes to the financial statements now provide additional details on the accounting of in-kind contributions, and the accounting change regarding Medical Insurance Plan premiums. After these adjustments, the main outstanding problem relates to the accounting for expenditure, as explained below.

33. As expenditure, UNHCR charged the amount of allocations provided through "letters of instructions", which are internal spending authorizations for administrative and operational projects. At the end of a fiscal year, the difference between the letters of instruction amounts and the disbursements made in the year is deemed equal to unliquidated obligations and reported as such in the financial statements, regardless whether or not such unliquidated obligations represent actual commitments. In other words, the expenditure amount reported in the financial statements represents not only disbursements and valid unliquidated obligations (funds committed through a purchase order, a contract or an agreement with an implementing partner), in compliance with the United Nations system accounting standards, but also the remaining balance, neither disbursed nor committed, under the concept of "unliquidated balances". In the absence of an audit trail, these are invalid figures.

34. Therefore note 2 (c) to the financial statements states that: "estimates are used in the context of expenditure recognition ... at the end of the financial period to determine the amounts to be retained in respect of unliquidated obligations", except that these are not really "estimates", but simply the difference between the budget as reflected in the obligated amounts, revised if need be at year-end, and the disbursements.

35. The actual unliquidated obligations, as opposed to those resulting from the mere difference between budget authorizations and disbursements, are backed by several reports issued from different systems or sources: those relating to purchase orders and contracts managed by headquarters are recorded and detailed in a report issued by a specific procurement information system (and not in the Financial and Management Information System (FMIS) general ledger); unliquidated obligations relating to travel and staff are recorded and detailed in a FMIS report (but again, not in the FMIS general ledger). In addition, \$37.8 million of field unliquidated obligations are not recorded in any financial system and are only backed by a manual compilation of information provided by the country offices. Such information would often not substantiate obligations in compliance with the United Nations system accounting standards.

36. At year-end, there are unavoidable differences between the unliquidated obligations amount reported in the financial statements and the amount of actual unliquidated obligations resulting from the above-quoted reports. Overall, in 2001, unliquidated obligations reported in the financial statements was \$74 million while the unliquidated obligations amount backed by "reports" was \$71 million, of which, as stated above, \$37.8 million in field unliquidated obligations were often not properly documented.

37. UNHCR agreed with the Board's analysis and concurred that expenditure should be more properly accounted for. However, it explained that changing the current accounting policy and accounting for unliquidated obligations in the general ledger would imply in-depth modifications of its current Financial and Management Information System. UNHCR is committed to achieving compliance with normal accounting practices when its new accounting software is implemented. As at May 2002, a date for such implementation was still to be set, and it is not likely to occur before 2004.

38. The Board, emphasizing the importance of compliance with the United Nations system accounting standards, and taking into account the commitment of UNHCR to attain it through a prompt implementation of a new information system, recommends that UNHCR modify its accounting policy and financial system to achieve an accurate accounting of disbursements and valid unliquidated obligations.

3. Write-off of losses of cash, receivables and property

39. UNHCR wrote off cash and accounts receivable amounting to \$67,214 during the year, in accordance with United Nations financial regulation 10.4. With regard to non-expendable property and other categories of losses, the amounts written off during 2001 were reported to the Board as follows (in United States dollars):

Table 3 Write-off of losses of property

| <i>Reason for loss</i> | <i>\$</i> |
|------------------------|----------------|
| Accident | 50 583 |
| Hijacking | 31 660 |
| Theft | 399 208 |
| Looting | 80 164 |
| Loss of property | 2 696 |
| Damaged/destroyed | 14 199 |
| Wear and tear | 2 823 |
| Total | 581 333 |

40. UNHCR provided the Board with explanations for all the losses and write-offs, and the Board is satisfied that appropriate action has been taken in the circumstances. However, refunds due are recognized only when the money is received; this does not allow for the best monitoring of amounts to be recovered.

41. The Board recommends that, whenever a party is held responsible for losses of cash, receivables and property and asked to refund the Organization,

UNHCR promptly record the related amounts on an accrual basis to improve control and accountability.

4. Ex gratia payments

42. At the Board's suggestion, UNHCR has disclosed in note 5 (b) to the financial statements an ex gratia payment for the transfer of \$856,127, coming from a national committee, in favour of a private charity. This charity, recently created under Swiss law with a former High Commissioner as founding president, aims to promote post-primary education for refugee children. In addition, the Board has noted that the Swiss foundation benefits from other UNHCR advantages, estimated for 2001 at \$250,000, for office space and support staff, as now disclosed in the note mentioned above. UNHCR has agreed to sign a service agreement with the Swiss foundation, and has indicated that it plans to terminate such services at the end of 2002.

43. The High Commissioner approved \$1,344,000 (of which \$838,391 was disbursed in 2001 and \$500,000 in May 2002) in ex gratia compensation to the families of three staff members who died in service in 2000.

C. Management issues

1. Implementing partner expenditure

Controls in place

44. United Nations agencies frequently entrust their operational projects to national entities as "implementing partners" under the "national execution and implementation arrangements" guidelines. UNHCR generally relies on non-governmental partners to implement projects; it undertakes direct implementation only "under exceptional circumstances". UNHCR indicated that \$283.1 million out of \$431.4 million (65.6 per cent) of operational expenditure was accordingly implemented by governmental or non-governmental partners, according to data available as of 15 April 2002. The proportion was 69.1 per cent in 2000 (\$311.1 million out of \$450.4 million). The figure of \$551 million in programme expenditure provided in the financial statements includes emergency projects of \$54 million, care and maintenance projects of \$193 million, repatriation projects of \$91 million, local settlements projects of \$89 million and resettlement projects of \$5 million and protection, monitoring and coordination projects of \$119 million.

45. Guidance to and monitoring of implementing partners is therefore of paramount importance and is achieved through the following procedures:

(a) UNHCR transfers responsibilities such as procurement, recruitment, accounting and reporting to its implementing partners. It controls the expenditure through their quarterly "Subproject monitoring reports" submitted to the concerned field office, which verifies the financial data, supporting documentation and monthly bank statements of the partner before forwarding the report to UNHCR headquarters. The reports are therefore the main monitoring tool;

(b) As a second step, following a Board of Auditors' recommendation, implementing partners have been requested since 1997 to submit external "audit certificates" obtained from local external auditors;

(c) Internal audits are carried out by the Office of Internal Oversight Services in the Field with the objective, inter alia, of determining whether implementing partners' accounting and internal control systems ensure completeness and accuracy of financial information submitted to UNHCR.

Control of implementing partner expenditure through the subproject monitoring reports

46. As mentioned by the Board in its previous reports, UNHCR signs with its implementing partners subproject agreements setting out the budget and a plan of cash advances that UNHCR will make to the partner. Actual advances depend on the progress achieved and the level of expenditures reported by the partner in the subproject monitoring report. UNHCR controls advances to the implementing partners through a project expenditure control (X21) account that is cleared once the subproject monitoring report has been verified by the field office.

47. The Board qualified its audit opinion on the 2000 financial statements¹ based on a limitation of scope in respect of a total of \$43.5 million of implementing partner expenditure due to absence or deficiencies of subproject monitoring reports. The amount was categorized as follows:

(a) The sum of \$8.5 million represented payments made to implementing partners in 2000, but for which headquarters had not received by June 2001 appropriately approved subproject monitoring reports;

(b) The amount of \$3 million represented implementing partners' expenditure that UNHCR could not check, owing to the fact that the country in which expenses were incurred denied UNHCR access to accounting records of governmental implementing partners;

(c) The sum of \$18 million represented subproject monitoring reports for which the Board identified, during its field missions, serious inadequacies in their verification and validation by UNHCR staff;

(d) The amount of \$14 million represented subproject monitoring reports reviewed at headquarters and for which the Board found that staff in charge of verifying the subproject monitoring report had provided limited assurance.

48. The situation for the 2001 financial statements is discussed below. Since the qualified opinion was due to issues relating to the subproject monitoring report, the Board has paid special attention in assessing to what extent UNHCR has improved its system of accountability in this respect.

49. Regarding expenditure not yet justified by the monitoring report, in its last report, the Board highlighted the considerable effort which allowed UNHCR to reduce by some \$186.5 million the total X21 balances involved. However, the Board noted that, at the end of June 2001, the X21 control account recorded uncleared advances to implementing partners totalling \$55.5 million for the years from 1994 to 2000. The Advisory Committee on Administrative and Budgetary Questions, having noted the progress achieved by UNHCR, trusted that further efforts would be made by UNHCR with regard to the

\$55.5 million outstanding advances to implementing partners (see A/56/436 (para. 4)).

50. As a result, in comparison with the above-mentioned \$55.5 million balance for 2000, the Board is pleased to note that efforts during 2001 have led to a further reduction of payments made prior to 2001 and not yet justified by subproject monitoring reports. Consequently, as at 21 June 2002, the outstanding payments made between 1994 and 2000 amounted to \$4.3 million. **The Board further encourages UNHCR to continue its efforts to obtain missing subproject monitoring reports.**

51. As regards payments made to implementing partners in 2001 and reported as expenditure in the 2001 financial statements, \$7.5 million was still not justified as at 21 June 2002.

52. As regards the case of the denial of access to accounts by one Member State, noted in reports by the Board of Auditors and the Office of Internal Oversight Services, the Advisory Committee on Administrative and Budgetary Questions stated "that the issue of denial of access to the accounting records of implementing partners, on which the Committee had commented in previous reports (see, for example A/53/513, paras. 95 and 96), continues to be a very serious problem with a potential for fraud. The problem should be thoroughly examined by the administration of UNHCR in order to determine whether the failure to provide access to accounting records is due to the lack of capacity of implementing partners or rather reflects the lack of will to cooperate with UNHCR. Should the latter be the case, the Committee requests that the issue be addressed at the highest level of UNHCR administration and, if necessary, be brought to the attention of the Secretary-General" (A/56/436, para. 6). UNHCR insistently tried in 2001 to access the original documents supporting the use by the Member State of the 2001 funds, which amounted to \$4.1 million. However, the Administration indicated that, further to a field mission carried out in June 2002, the governmental partners have given assurance that their accounts would be open.

53. The Board recommends that UNHCR verify without further delays the expenditure reported by the governmental partners.

54. As regards the effectiveness of checks performed by the field officers on the subproject monitoring reports, the Board is pleased to report on improvements noted during its field visits: regular financial monitoring visits are made to assess the reliability of implementing partners' accounting, budgetary and internal control systems, in order to obtain reasonable assurance that the figures reported are complete and accurate. Programme officers still report numerous issues, which they are increasingly monitoring, such as:

(a) Lack of expertise from non-governmental organizations – insufficient knowledge of or compliance with UNHCR procedures;

(b) Difficulties in reconciling implementing partners' accounts and incompatibility between the accounting system of UNHCR and of the non-governmental organizations;

(c) Difficulties in verifying expenditures for non-governmental organizations' international staff and overhead costs (difficulty in accessing supportive documents), and lack of supporting documentation;

(d) Late submission of subproject monitoring reports, mistakes in the contents and attempts to manipulate cost figures;

(e) Non-authorized budget adjustments. Cancellation of activities without consulting UNHCR;

(f) Incorrectness of currency implementation (United States dollars instead of local currency) or impossibility to track some disbursements, owing to exchange rate variations;

(g) No separate bank accounts. Substantial number of disbursements in cash;

(h) Payments by the implementing partners for services or goods disbursed in advance;

(i) Difficulties in getting the unspent balances from the implementing partners. Non-refund of miscellaneous income;

(j) Absence of narrative report; failure to achieve an objective.

55. For 70 per cent of an expenditure of \$48 million in a sample of 24 subproject monitoring reports that the Board reviewed at UNHCR headquarters, a reasonable assurance was provided by the monitoring of the amount reviewed. The remaining 30 per cent (\$14.6 million) was either not properly signed by the authorized UNHCR staff or the two officers required by UNHCR regulations, or the figures were altered and crossed out. In this respect, the Board welcomed the new format for the reports, issued in April 2002, to the extent that it is likely to improve the accountability of both the implementing partners and UNHCR. It clearly states the meaning of the certification made by the partner (certifying that the information in the report is based on its accounts and reflects the financial situation of the project and that funds have been used in accordance with the project agreement) and the extent of the verification carried out by UNHCR (completeness, accuracy and compliance with the agreement).

56. The Board encourages UNHCR to continue its efforts in verifying subproject monitoring reports effectively.

Control of implementing partner expenditure through audit certificates

57. The Board examined both rules and practices with a view to assessing whether: (a) the rules were relevant vis-à-vis their purpose as defined in UNHCR Manual, that is, to ensure that "the funds provided by UNHCR have been used for the purpose and intent, and in accordance with, the budgetary provisions of the agreement signed between UNHCR and the implementing partner"; and (b) the certificates were issued in a timely manner and followed up in such a way that action can be taken when necessary.

58. To carry out its review, the Board focused on audit certificates related to 2000 expenditure entrusted to international non-governmental organizations (\$148 million), Governments (\$76.6 million) and local non-governmental organizations (\$68.7 million). The focus is not on the latest, 2001 expenditure, since the deadline for their submission is six months after liquidation date of the project or after the international non-governmental organizations fiscal year, that is, after the present report was to be issued. Out of the 621 audit certificates received as at 25 March 2002, the Board reviewed 375 certificates totalling \$123.8 million (42 per cent of the 2000 operational expenditure executed by non-governmental organizations and Governments).

59. Audit certificates are intended to provide UNHCR with the assurance that expenditure has been incurred for the purpose of the project. Since expenditure is reported in the subproject monitoring reports, this financial report should be the one audited. Yet, this is thus far the case only for national non-governmental organizations. For this category, auditors have had to audit the subproject monitoring report itself since 1998 and to produce a management letter since fiscal year 2001. However, despite the latest UNHCR efforts, compliance remains quite unsatisfactory, since for 85 per cent of the expenditure reviewed in the sample, the monitoring report was still not mentioned in the audit certificates.

60. For international non-governmental organizations, UNHCR accepts a "single audit", carried out by the non-governmental organization's external auditor. The only requirement is that UNHCR funding be clearly identified in the non-governmental organization's consolidated audited financial statements, and that the opinion clearly indicates that UNHCR funds were duly included in the "audit". Since the monitoring report is not included in the scope of the independent audit, UNHCR receives no assurance from the external auditors of international non-governmental organizations that the figures therein are accurate. These rules, already deficient, were not even complied with in a significant proportion in that audit certificates covering 33 per cent of the expenditure reviewed by the Board did not clearly state that UNHCR funds were used in accordance with agreements.

61. For governmental partners, requirements call for a "certificate issued by the appropriate government audit authority, together with such comments as the auditor may deem appropriate in respect of project operations generally and, in particular, the financial situation as reported by the Government". But 95 per cent of the 56 certificates, for an amount of \$31.6 million that the Board reviewed, do not mention the subproject monitoring report data nor provide any comment, and therefore give no assurance that the UNHCR requirement has been complied with.

62. The overall result of both rules and practice for the three categories of partners is that, out of the \$123.8 million covered by certificates reviewed by the Board, \$106 million lacked subproject monitoring report audit (86 per cent). Of the same \$123.8 million, \$27.6 million also had no clear certification of compliance with rules for the use of funds. For local non-governmental organizations, the Board considers that the gap between the certification rules and their implementation remains at an unacceptably high level of risk, while non-compliance with UNHCR rules regarding international non-governmental organizations and governmental partners is such that UNHCR

has insufficient assurance through audit certificates that funds are properly used.

63. **The Board recommends that UNHCR: (a) mobilize more adequate means to ensure timely and full compliance with existing rules; (b) assess the feasibility and cost-effectiveness of adjusting present audit requirements, such as expanding the procedure for local non-governmental organizations to cover international non-governmental organizations and governmental partners, including independent subproject monitoring report audit certification and management letter.**

Auditor selection

64. Regarding the independence and expertise of auditors for governmental projects, UNHCR directives are that the Supreme Audit Institution or the Ministry in charge of Finance should conduct the audit. One tenth of the 2000 UNHCR-related expenditures by Government were audited in accordance with this rule. Over nine tenths of the audit coverage was entrusted by Governments to private firms or ministries other than the ministry in charge of finance. Timeliness is, of course, of the essence. For instance, in one country, the audit of the project implemented by a governmental authority is issued as part of an overall Auditor-General's report issued only every two or three years. UNHCR has, in this case, discussed the possibility of ad hoc arrangements, but so far without success.

65. Most non-governmental organizations choose and pay their own auditors. However, some UNHCR field offices directly engage qualified external auditors, after a competitive process, in order to ensure that the audits are conducted in a professional and non-biased manner.

66. **The Board recommends that UNHCR: (a) with the assistance of the Office of Internal Oversight Services, define the requirements for government audits and the resulting audit certificates and provide guidance, as has been done for local non-governmental organizations; (b) when a public audit institution is not available, invite Governments to engage private audit firms selected to perform the audit of government-implemented subprojects; (c) include in its guidelines specific procedures and predetermined criteria to ensure that the local external auditors possess the required independence, integrity and technical competence and are appropriately monitored when they come from the private sector, and that they are provided with adequate audit terms of reference.**

Audit resources

67. There are no guidelines on audit funding. UNHCR is therefore unable to ensure consistency in the funding and scope of audits, and to monitor the cost-effectiveness of the audit function. Government partners usually provide the audits free of charge, while international non-governmental organizations finance the audits directly or through UNHCR funding for overhead costs (for which no detailed breakdown is required). National non-governmental organizations charge the cost of the external firm of auditors to the project.

68. The Board recommends that UNHCR request implementing partners to budget and disclose the resources allocated for certification in all cases and to develop guidelines for an effective monitoring of audit resources.

Monitoring of deadlines for issuance of audit certificates

69. Completion deadlines were unified in January 2001 for governmental partners and national non-governmental organizations which are now requested to submit audit certificates within six months after the liquidation date of the project. International non-governmental organizations are requested to produce their audit certificates within six months at the end of their fiscal year, which may or may not be a calendar year. Therefore, the bulk of audit certificates can realistically be expected more than six months after the liquidation date.

70. However, this is not the case for the majority of the funds. With regard to audit certificates on 2000 expenditure, the overall situation as at 25 March 2002 was as follows: out of the total of expenditure executed in 2000 by non-governmental organizations and Governments (\$293.2 million), the audit certificates received covered \$204.7 million (70 per cent). This means that 15 months after the end of 2000, 30 per cent of the 2000 expenditure had not been covered by audit certificates. This low rate is a matter of concern. At the same date, no audit certificate had been submitted for about 23 per cent of the expenditure incurred in 1998 (representing \$81 million) and for 17 per cent of the expenditure incurred in 1999 (\$70 million).

Table 4 Submission of audit certificates

| <i>Year</i> | <i>Expenditure (millions of United States dollars)</i> | <i>Percentage of expenditure covered by audit certificates received by 30 November, year+1</i> |
|-------------|--|--|
| 1998 | 339 | 48 |
| 1999 | 401 | 43 |
| 2000 | 293 | 47 |

71. While acknowledging that in some circumstances audits cannot be performed, the Board notes with concern the lack of improvement over 1998 and recommends that UNHCR enforce deadlines for submission of audit certificates.

Table 5 Results of audit certificates

| <i>Fiscal year 2000</i> | <i>Qualified opinion</i> | | <i>Significant finding</i> | |
|--|--|----------------------------------|--|----------------------------------|
| | <i>(millions of United States dollars)</i> | <i>Percentage of expenditure</i> | <i>(millions of United States dollars)</i> | <i>Percentage of expenditure</i> |
| Governments | - | - | 0.2 | 0.7 |
| National non-governmental organizations | 0.5 | 3 | 5.1 | 29 |
| International non-governmental organizations | 1.4 | 2 | 20 | 26 |
| Total | 1.9 | 1.5 | 25.3 | 20 |

72. In the audit certificates covered by the Board's review, significant findings were provided for \$25.3 million expenditure (table 5). A qualified opinion was expressed for 1.5 per cent of the expenditure. UNHCR has acted upon this situation in some countries: in one case, the recommendations made by the auditors led to the cancellation of the sub-agreement and to the recovery of funds from one implementing partner. In another case, a plan was prepared to strengthen the capacity of a non-governmental organization to deal with urban refugees and to improve its internal controls; when performance did not improve to the required level, a new implementing partner was selected to replace that non-governmental organization. Other field offices did not provide proof of audit follow-up.

73. **The Board recommends that UNHCR: (a) monitor corrective action taken by field offices in cases of audit certificates with qualifications or major findings, and document the follow-up; and (b) consider the establishment of a comprehensive database on local audit resources history and results to facilitate audit monitoring and risk assessment.**

74. In conclusion, despite valuable progress undertaken in the recent period, the Board is of the opinion that the audit certificates still do not provide sufficient assurance of the proper use of funds.

Control of implementing partner expenditure through field visits undertaken by the Office of Internal Oversight Services

75. The Board relies heavily on UNHCR internal audit by the Office of Internal Oversight Services. It reviewed the reports of the Office of Internal Oversight Services on implementing partners completed in 2001, which covered 128 implementing partners with expenditure amounting to \$170.7 million. The Office of Internal Oversight Services indicates whether a reasonable assurance of proper use of funds entrusted to implementing partners can be obtained, and whether the implementing partner accounting system and internal controls are satisfactory. Out of \$170.7 million, the Office of Internal Oversight Services found that it could not have a reasonable assurance for \$53.9 million (31.6 per cent), that the accounting systems were

not satisfactory for \$52 million (30.5 per cent) and that the internal controls were inadequate for \$44.9 million (26.3 per cent). These findings were confirmed by the few field visits implemented by the Board.

76. The Board notes with grave concern the high level of deficiencies among implementing partners, as audited by the Office of Internal Oversight Services.

2. Cash management

Exchange risk management

77. Since 2000, pledges for contributions made in currencies other than the United States dollar have been recorded at the United Nations exchange rate at the time of recording the pledge. UNHCR runs the risk of obligating pledges at a dollar value which, due to exchange rate fluctuations, will not fully materialize at the time of payment. Such fluctuations may substantially affect income insofar as UNHCR does not hedge against the related risks. Indeed, loss on exchanges on pledges recorded in the 2001 financial statements amounted to \$12.4 million.

78. The Board recommends that UNHCR manage exchange rate risks by adopting a more proactive stance, as do other United Nations organizations dealing with similar issues.

79. As at 31 December 2001, cash and term deposits amounted to \$140.5 million deposited in some 30 headquarters and 400 field office bank accounts. There were no available written contracts for headquarters bank accounts. UNHCR was therefore unable to provide comparisons between financial institutions in terms of costs or earnings. Since the Board's review, UNHCR has requested all banks handling headquarters accounts to provide a copy of their General Conditions. The Board also noted that all headquarters banks were retained without competitive bidding.

80. The Board recommends that UNHCR: (a) set and regularly update a comprehensive database in respect of bank services, based on written agreements; and (b) launch competitive bidding for all headquarters bank accounts in order to obtain the best condition and services.

81. The Board also noted that interest obtained on the 400 field office accounts amounted to \$120,150, while bank charges for those accounts reached \$684,727, which may leave room for more favourable banking conditions. UNHCR indicated that, out of \$684,727 of bank charges, \$150,000 was incurred with two banks that are in a monopolistic position.

82. The Board recommends that UNHCR continue its efforts to streamline and optimize the management of its field office banking operations.

Bank signatories

83. UNHCR officers act as bank signatories and provide the last internal control before UNHCR cash is disbursed. The list of bank signatories as reviewed by the Board at year-end 2001 disclosed that rules were not always complied with. While two Professionals (or, when circumstances so warrant, at

least one Professional), or higher level staff are required by UNHCR financial rule 5.11, one General Service staff member can be one of the two bank signatories for all headquarters accounts. In 10 field locations, General Service staff members were acting as single signatories. For 21 bank accounts, signatories were no longer UNHCR staff members and sometimes could act alone.

84. The Board recommends that UNHCR ensure that all bank signatories are UNHCR staff, designated in compliance with its rules.

3. Information systems of the Office
of the United Nations High Commissioner for Refugees

85. As stated in the previous report of the Board, in 1998, UNHCR launched the Integrated System Project to provide the Organization with an "enterprise resource planning", integrated management tool. In 1999, it purchased a commercial software package. A supplier was selected for implementing the project on the basis of a cost proposal of \$17.9 million to cover all external costs for the changeover, to be completed by 2002. The entire project implementation was to be spread over 15 quarters at a global cost of \$34 million, including internal costs. In June 2001, the new leadership of UNHCR put the Integrated System Project on hold, considering, rightfully, that it failed to comply with best practices for project management (such as for project lifecycle, requirements, plan, budgeting costs, monitoring costs against targets and deliverables), as highlighted by the Board in its last report. As a result, the current UNHCR information system continues to be used until the Integrated System Project is restarted or another solution rolled out. In this context, the Board assessed the risks of the current Financial and Management Information System (FMIS) and reviewed the status of the Integrated System Project, together with the financial impact of the decision to put the project on hold.

86. Since the Board's review in January 2002, measures have been taken by UNHCR with a view to addressing urgent preliminary issues. An Information Resource Council has been established, and so has a line of command for FMIS.

Financial Management Information System

87. FMIS is not an integrated system. Each application is "isolated" and data can only be exchanged via interfaces. This configuration and the excessive number of applications expose UNHCR to a considerable risk of errors, notably with regard to the transmission of data. Furthermore, while it is based on a technology first rolled out in the 1980s, FMIS has not been upgraded in line with the same generation (better interfaces, compatibility with recent operating systems, etc.) and the gap between it and its users' functional requirements is widening. Despite the limited progress made with the Integrated Systems Project, FMIS has not been upgraded and enhanced.

88. The Board recommends that, with a view to maintaining state-of-the-art reliability and improving the cost-efficiency of its financial and accounting management, UNHCR address the current functionality deficiencies and define a clear development strategy needs for FMIS, factoring in: (a) the technological delays that have built up with FMIS developments over the past few years; (b) the decisions that will be taken to restart the Integrated Systems Project or a similar project and its provisional roll-out date. The Board further

recommends that as long as FMIS produces UNHCR accounts, a risk estimation procedure be implemented to provide the management with the indicators required to take decisions effectively.

89. UNHCR does not have the staff needed to maintain the quality of service required for its applications. A knowledge transfer and training process is under way in the light of forthcoming retirements, but expert knowledge of the tools and functionality is still restricted to too few people. Furthermore, the concentration of knowledge heightens the risk of one or more members of the team becoming indispensable and the organization having no backup solution. While recognizing that a separation of development, maintenance, support and production functions is a valid approach in addressing many software system shortfalls, UNHCR considers the issue of data reliability to be a technical issue and not a structural one.

90. The Board recommends that UNHCR: (a) allocate the human and budgetary resources required to maintain the current system; and (b) separate the support, maintenance, development and production tracking functions to ensure the reliability of accounting and financial data.

Integrated System Project

91. Management tasked a working group to draw up an effective strategic plan (Corporate Operating Model) redefining the project goals and objectives. However, no work was undertaken in 2001. Following the Board's review, UNHCR issued, in April 2002, a report on "Readiness assessment and immediate action plan for enterprise resource planning implementation in the Finance and Supply Chain Divisions". As at 8 May 2002, a final decision regarding the restart of the Integrated System Project had not been taken.

92. The cost of the project, as estimated in the project charter released by the selected supplier in March 2001, has increased from \$34 million to over \$42 million, owing to external costs having increased from \$17.9 million to \$27 million.

93. At the end of 2001, Integrated System Project expenditure amounted to \$12.9 million – 38 per cent of the initial budget – with no operational result. The costs resulting from the suspension of the project in June 2001 have been estimated by the Board at about one tenth of that amount. The main items of expenditure between June and December 2001 are presented below:

(a) The hardware and software purchased for the project are not being used. Although UNHCR does not depreciate its assets, such investments would generally be amortized over five years (linear), representing the average lifetime of investments. The longer it takes for the project to restart, the shorter the remaining useful life of the assets. It is not even certain that the hardware will still be suitable for future use;

(b) Maintenance costs continue to accrue each month, despite the fact that the project has been put on hold. They represent a significant percentage of the project's recurrent costs. Hardware and software maintenance are billed at the same rate as if the tool were operational. Contrary to best practices, scaled-down maintenance services until final project delivery were not

negotiated at the inception stage. The cost of the freeze for maintenance over the past six months may be estimated at around 50 per cent of the annual bill, that is, \$160,770;

(c) A total of 412 training modules were initially purchased from the software supplier in June 1999, and had been utilized at the beginning of 2001. A further 150 units were purchased in March 2001. Approximately 50 of these 150 training units have been used to date. As stipulated in the contract, the remaining units should have been used before 28 February 2002. As they were not, the related losses amounted to \$43,400. Some trainees have left the project and their departure represents a loss in terms of know-how. Since the first training courses held in 1999, trainees have probably lost most of the knowledge acquired, as they have not used the software. If the project resumes, a number of courses that were already provided will have to be repeated.

94. The Board recommends that UNHCR negotiate a discount on hardware and maintenance services until the project has resumed; and update the inventory of the skills acquired through the training courses, in order to optimize in due time any resumption of such trainings.

95. If and when the project is restarted, new costs will have to be budgeted, or losses accounted for, ranging from some tens of thousands of dollars up to several millions if the current solution is dismissed and another package and supplier for implementation selected. These potential losses and costs are to be compared to the \$42 million quoted above, which were the updated Integrated System Project estimate as provided by the supplier before the project was put on hold.

96. The United Nations Secretariat has developed its IMIS at a cost of over \$80 million over the past decade, with a view to answering the needs of most United Nations entities. Among several such other recent developments, another United Nations agency has simultaneously prepared, in 2002, a new plan to spend some \$100 million on a similar system.

97. As already noted by the Board in its previous report, UNHCR had initially looked into the possibility of using IMIS. Following an analysis of its functional requirements and a gap analysis, UNHCR discounted this possibility, as it estimated that IMIS would require too many management developments to bring it into line with its specific needs. In hindsight, the question remains open as to whether the failure to provide a timely solution, and the travails before implementing one, have not been much more expensive than opting for IMIS.

98. Regarding intra-United Nations information and communication technology coherence, the distinction is made by UNHCR between an "information and communication technology approach" – the information and communication technology management strategy – and an "enterprise resource planning approach", the narrower enterprise resource planning, "business support" solution. In terms of the information and communication technology approach, UNHCR is in contact with the rest of the United Nations system through inter-agency groups and the International Computing Centre. In terms of the enterprise resource planning approach, progress at other agencies is being followed by UNHCR with the Food and Agriculture Organization of the United

Nations, the International Civil Aviation Organization, the International Fund for Agricultural Development, the International Labour Organization, the International Telecommunication Union, the International Monetary Fund, the United Nations International Drug Control Programme, the United Nations Educational, Scientific and Cultural Organization, the United Nations Children's Fund, the United Nations Development Programme, the Universal Postal Union, the World Health Organization, the World Food Programme, the World Intellectual Property Organization, the World Bank, the World Meteorological Organization, the World Trade Organization – a number of which are known to consider or develop their own enterprise resource planning solutions.

99. The Board expresses grave concern and reservations about this concurrence of a number of very costly information and communication technology systems within the same United Nations system, at the expense of the same stakeholders, the Member States, covering the same geographical areas, under similar rules and regulations, towards the same global ends.

100. The Board recommends that UNHCR: (a) consult with the United Nations Secretariat and other relevant United Nations entities to ensure that, in terms of cost-benefit, the present diversity of information systems approaches is in the best interest of Member States and of the beneficiaries of United Nations programmes; and (b) ascertain that there are no ready-made solutions, even at the cost of alterations in current UNHCR procedures, preferably within the United Nations system.

4. Cases of fraud and presumptive fraud

101. UNHCR has reported no cases of fraud in 2001. The findings of the investigation mentioned in paragraph 109 of the Board's report for 2000 (A/56/5/Add.5) were reported to the General Assembly on 21 December 2001 (A/56/773).

D. Acknowledgement

102. The Board wishes to express its appreciation for the cooperation and assistance extended to the auditors by the High Commissioner and his staff.

(Signed) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(Signed) Guillermo N. **Carague**
Chairman, Philippine Commission on Audit

(Signed) François Logerot
First President of the Court of Accounts of **France**

27 June 2002

ANNEX

Follow-up on action taken by the Office of the United Nations High Commissioner for Refugees to implement the recommendations of the Board of Auditors in its report for the year ended 31 December 2000^a

The Board has followed up on the actions taken by UNHCR to implement the Board's recommendations made in the context of its report for the year ended 31 December 2000. Table A.1 summarizes the status of implementation of all the previous recommendations while table A.2 details specifically those recommendations not implemented and those recommendations under implementation which require further comment.

A total of 13 recommendations were made in the audit for the year 2000. Of those, six (46 per cent) were implemented and seven (54 per cent) were under implementation.

Table A.1 Summary of status of implementation of recommendations for the year ended 31 December 2000

| <u>Topic</u> | <u>Implemented</u> | <u>Under Implementation</u> | <u>Not Implemented</u> | <u>Total</u> |
|-----------------------------|------------------------|--|------------------------|--------------|
| <u>COMPONENT A</u> | | | | |
| Financial Issues | | | | |
| Programme management | | Para. 11 (a) | | |
| Accts and financ. reporting | Para. 53 | Para. 11 (b) | | |
| Sub - Total no. | 1 | 2 | 0 | 3 |
| Sub - Total % | 33.3% | 66.7% | 0% | 100% |
| <u>COMPONENT B</u> | | | | |
| Management Issues | | | | |
| ICT | Para. 70, 87, 90 | Para. 11 (c) Para. 11 (d) | | |
| Programme management | Para. 105 Para. 107 | Para. 11 (e) Para. 11 (f) Para. 11 (g) | | |
| Sub - Total no. | 5 | 5 | 0 | 10 |
| Sub - Total % | 50% | 50% | 0% | 100% |
| TOTAL - No. | 6 | 7 | 0 | 13 |
| TOTAL % | 46% | 54% | 0% | 100% |

^aOfficial Records of the General Assembly, Fifty-sixth Session, Supplement No. 5E (A/56/5/Add.5).

Table A.2 Details on previous recommendations under implementation or not implemented for the year ended 31 December 2000

| <i>Management</i> | | | <i>Comments of the Board</i> |
|--|---|--|---|
| <i>Component/area of concern</i> | <i>Recommendation</i> | <i>As at 30 April 2002</i> | |
| | | <i>Specific management action/comments</i> | |
| 1. Project financial oversight, para. 30 | Strengthen its oversight of field offices to ensure that they undertake a thorough verification of subproject monitoring reports, including the verification of supporting documentation and bank statements. | <p>In December 2001, UNHCR issued revised instructions and guidance on subproject monitoring reports. The comprehensive revision of section 6.5 of chapter 4 of the UNHCR Manual formed part of the ongoing update of the Manual and was sent to all UNHCR offices. This revision provided more extensive procedural guidance for field offices on how to process, verify and accept the reports. The notion of formal annual monitoring and reporting plan with implementing partners was introduced in order to ensure a systematic monitoring, including expenditure verification. The revision also emphasizes the importance of verification and acceptance of the reports and defines (...).</p> <p>In parallel, the financial part of the format of the report has been amended to incorporate additional fields whereby partners are to disclose separately any income received (e.g. interest earned). The new format also includes additional lines that provide more extensive explanations on the certification by the implementing partner and the extent of the verification made by UNHCR (completeness, compliance and accuracy with the sub-agreement).</p> | Under implementation. The Board, in view of continuing problems in the verification of subproject monitoring reports, as indicated in the present report, welcomes the recent improvements in strengthening controls carried out by field offices. It notes that the revised instructions issued in December 2001 by UNHCR are a step towards a strengthened verification of the financial data submitted by the implementing partners. |

| <i>Management</i> | | | <i>Comments of the Board</i> |
|---|--|--|---|
| <i>Component/area of concern</i> | <i>Recommendation</i> | <i>As at 30 April 2002</i> | |
| | | <i>Specific management action/comments</i> | |
| Audit certificates, para. 38 | Ensure that field offices review audit certificates received in respect of projects and follow up any significant issues that arise. | As previously mentioned to the Board of Auditors, UNHCR has already implemented this recommendation. The revised UNHCR Manual, chapter 4, section 5.1 and appendix 8(c), contains guidelines to field offices for the review of audit certificates in respect of projects implemented by implementing partners. (...) UNHCR, through its Internal Audit Service, is developing a database of its major partners implementing projects with an aggregate value amounting to over \$1 million. | Under implementation. The Board, in view of its continuing comments on audit certificates in the present report, welcomes the recent developments. |
| Information and Communication Technology: Integrated System Project, para. 64 | Establish for the Integrated System Project clearly defined, ranked benefits that are quantified as far as possible, in order to establish realistic milestones against which progress can be monitored. | Following suspension of the Integrated System Project in June 2001, work was undertaken to define the framework for a Corporate Operating Model. (...) One of the initial tasks will be to clearly define the integration points between the priority areas (Finance and Supply Chain) and the rest of the house (Operations and Human Resources). This work will form the basis for the Corporate Operating Model, the remaining components of which will be addressed at a future point. (...) Before a decision is taken to restart the project, benefits will be re-examined in the light of the (initial) reduced scope and will take into consideration the integration between Finance, Supply Chain, Human Resources and Operations. | Under implementation. The Board notes in the present report that several months elapsed before any action was taken after its previous report, and that the existing financial information system is not properly maintained. |
| ICT project, para. 81 | Establish and maintain a single line of project management | UNHCR already acknowledged that the frequent changes in the project governance structure have been a major | Under implementation. The Board welcomes the intentions of |

| <i>Management</i> | | | <i>Comments of the Board</i> |
|--|---|--|---|
| <i>Component/area of concern</i> | <i>Recommendation</i> | <i>As at 30 April 2002</i> | |
| | | <i>Specific management action/comments</i> | |
| | through which staff report on all aspects of the Integrated System Project. | problem. Once the project resumes, the position of the Project Manager will be re-advertised and all project staff will report to this Manager (...). | UNHCR. |
| Appropriateness of assistance projects, para. 97 | Review the appropriateness of engaging in projects which are not of direct assistance to refugees, and routinely set clear milestones against which to measure progress and assess when its mission was complete. | (...) the High Commissioner (...) is presently inclined to move away from the concept of Special Operations. In doing so, he has taken into account the position of some key donors, and the comments of the Advisory Committee on Administrative and Budgetary Questions in its report (A/AC.96/950/Add.1). Based upon a 2002 review, a decision will be taken on whether the procedures suggested for the 2003 programme review need adjustment/correction before standardization and inclusion in chapter IV and in specific instructions (...). last action planned by UNHCR in response to this recommendation – the incorporation of guidance on setting milestones into the guide for the use of work plans – is developed below in the update on the same proposed course of action, under the response to recommendation 8 (a). | Under implementation |
| Statistics on refugees, para. 100 | Establish a suitable system to ensure that accurate information is maintained on the size and characteristics of the refugee population. | In line with the interim focus on the non-information technology components and initiatives of PROFILE, support continued to be provided, both by Headquarters and by field-based regional support-staff, to a significant number of ongoing registration operations in the field (...). Management decided in February 2002 that (...) a | Under implementation The Board notes the forthcoming developments. |

| <i>Management</i> | | | <i>Comments of the Board</i> |
|--|--|---|---|
| <i>Component/area of concern</i> | <i>Recommendation</i> | <i>As at 30 April 2002</i> | |
| | | <i>Specific management action/comments</i> | |
| | | business case should be prepared in order to set the rationale for any decision on information technology systems development more clearly in the context of the strengthened registration and population data management policies and practices (...) A business case for PROFILE (...) is expected to be considered by senior management in mid-May 2002. | |
| Project objective and indications, para. 103 | Include clearly stated and quantified objectives and outputs in subprojects agreements and produce work plans incorporating key milestones and target dates. | The (...) "Project Planning in UNHCR: A practical guide on the use of objectives, outputs, and indicators" was sent to the field during March 2002, and field offices are sharing the guide with implementing partners (...). | Under implementation The Board welcomes the guide and will monitor developments. |

CHAPTER III

AUDIT OPINION

We have audited the accompanying financial statements, comprising statements I to III, schedules 1 to 5, and the supporting notes to the accounts of the voluntary funds administered by the United Nations High Commissioner for Refugees for the period from 1 January to 31 December 2001. These financial statements are the responsibility of the High Commissioner. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the common auditing standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, and as considered by the auditor to be necessary in the circumstances, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the High Commissioner, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the audit opinion.

In our opinion, the financial statements present fairly, in all material respects, the financial position at 31 December 2001 and the results of operations and cash flows for the period then ended in accordance with the United Nations High Commissioner for Refugees' stated accounting policies, set out in note 2 to the financial statements, which were applied on a basis consistent with that of the preceding financial period.

Without qualifying our opinion above, we draw attention to our findings on implementing partner expenditure. Although we noted significant improvements, we were concerned about the effectiveness of internal controls and procedures as well as the adequacy of assurance obtained by UNHCR that funds had been properly used for the purpose intended.

Further, in our opinion, the transactions of the United Nations High Commissioner for Refugees that we have tested as part of our audit have, in all significant respects, been in accordance with the Financial Regulations and legislative authority.

In accordance with article XII of the Financial Regulations, we have also issued a long-form report on our audit of the financial statements of the voluntary funds administered by the United Nations High Commissioner for Refugees.

(Signed) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(Signed) Guillermo N. **Carague**
Chairman, Philippine Commission on Audit

(Signed) François **Logerot**
First President of the Court of Accounts of France

27 June 2002

CHAPTER IV

STATEMENT OF THE HIGH COMMISSIONER'S RESPONSIBILITIES
AND
APPROVAL OF THE FINANCIAL STATEMENTS

The United Nations High Commissioner for Refugees is ultimately responsible for the content and integrity of the financial statements contained in the accounts of the voluntary funds administered by the United Nations High Commissioner for Refugees which are submitted to the Executive Committee of the High Commissioner's Programme and to the General Assembly.

To fulfil its responsibility, UNHCR operates within prescribed accounting policies and standards and maintains systems of internal accounting controls and procedures to ensure the reliability of financial information and the safeguarding of assets. The internal control systems and financial records are subject to reviews by the Office of Internal Oversight Services and the United Nations Board of Auditors, during their respective audits.

In this context, the following financial statements, comprising statements I to III, schedules 1 to 5, annexes I and II, an appendix and supporting notes, were prepared in accordance with UNHCR financial rules (A/AC.96/503/Rev.7) and the United Nations common accounting standards. In the opinion of management, the accompanying financial statements present fairly the financial position of the Office as at 31 December 2001, as well as the results of its operations and its cash flows of individual programmes, funds and accounts for the year then ended.

The accounts are hereby

Approved:
(Signed) Ruud **Lubbers**
United Nations High Commissioner for Refugees

Certified:
(Signed) Wolfgang **Milzow**
Controller and Director, a.i.
Division of Resource Management

2 May 2002

CHAPTER V

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2001
NOTES TO THE FINANCIAL STATEMENTS

*(see document A/AC.96/962, Voluntary Funds Administered by the United Nations
High Commissioner for Refugees)*