

PART II

REPORT OF THE EXTERNAL AUDITOR



National Audit Office

2004-2005

External Auditor's Report to the Directing Council

International Audit

The United Kingdom National Audit Office (NAO) provides an external audit service to the Pan American Health Organization (PAHO) and the Institute of Nutrition of Central America and Panama (INCAP). The External Auditor, Sir John Bourn, has been appointed by the Directing Council of PAHO in accordance with Regulation XIV of the Financial Regulations. In addition to certifying the accounts of PAHO and INCAP, he has authority under the mandate to report to the Directing Council on the economy, efficiency and effectiveness with which the Organization has used its resources.

The NAO provides external audit services to international organizations, working entirely independently of its role as the Supreme Audit Institution of the United Kingdom. The NAO has a dedicated team of professionally qualified staff with wide experience of the audit of international organizations.

The aim of the audit is to provide independent assurance to the Directing Council; to add value to the organization's financial management and governance; and to support the objectives of the Organization's work.

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Report of the External Auditor on the Financial Statements of the Pan American Health Organization for the Financial Period 1 January 2004 to 31 December 2005

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EXECUTIVE SUMMARY

OVERALL RESULTS OF THE AUDIT

1. I have audited the Financial Statements of the Pan American Health Organization (PAHO) in accordance with the Financial Regulations and in conformity with the Common Auditing Standards of the Panel of External Auditors of the United Nations, the Specialized Agencies and the International Atomic Energy Agency. I have provided a separate audit opinion and report in relation to the Financial Statements of the Institute of Nutrition of Central America and Panama (INCAP).
2. My examination revealed no weaknesses or errors which I considered material to the accuracy, completeness and validity of the Financial Statements as a whole and I have placed an unqualified audit opinion on the Organization's Financial Statements for the biennium ended 31 December 2005.
3. Observations and recommendations arising from the audit are set out in summary below and in the section of this report entitled Detailed Findings.

ON THE OVERALL FINANCIAL POSITION OF THE ORGANIZATION

Regular Budget

4. The Financial Statements report that for 2004-2005 the Organization obligated \$175,259,824 or 94 percent of the Effective Working Budget, excluding the WHO Regular Budget element of \$72,730,000. After adjustments, the Organization recorded a net excess of income over expenditure on the Regular Budget amounting to \$5,998,568 compared with \$15,634 for 2002-2003.
5. The collection rate for quota contributions for the current period of 73 percent was lower than the previous biennium; however there was an increase from 66 percent to 80 percent in the collection rate for quota arrears. Of the \$61,740,124 outstanding at 31 December 2005 on quota assessments for the current and prior periods, some \$15.6 million (25 per cent) had been received by 31 March 2006.
6. The Working Capital Fund balance was \$11,608,634 at 1 January 2004. Following the \$5,998,568 excess of income over expenditure and a transfer to the Capital Equipment Fund of \$3,400,000, this balance increased to \$14,207,202 as at 31 December 2005. The authorized level of the Working Capital Fund was increased from \$15,000,000 to \$20,000,000 by the 44th Directing Council (2003), and thus the Working Capital Fund balance as at 31 December 2005 was within the authorized level.

Total Funds

7. Total PAHO expenditure across all funds increased by 9.5 percent from \$717,888,896 in 2002-2003 to \$786,316,900 in 2004-2005. This increase reflects the increased activity of the Trust Funds, the Expanded Program on Immunization and WHO Other Funds. Total fund balances increased by \$9,714,508 during the biennium and, despite the collection of prior years' assessed contributions increasing by \$14,196,364

compared to the previous biennium, net cash and term deposits decreased by \$37,494,781 as reported in Statement III.

ON THE FINANCIAL POSITION OF THE CENTRES (CAREC, CFNI AND INCAP)

8. The overall financial position of the Caribbean Epidemiology Center, CAREC, improved slightly in 2004-2005. The balance on CAREC's Working Capital Fund decreased from \$945,845 to \$672,687, while the Trust Fund balance increased by \$296,914 despite a decrease in income of 9 percent to \$6,344,584.
9. The overall financial position of the Caribbean Food and Nutrition Institute, CFNI, improved in 2004-2005. Although the overall funds balance decreased by \$21,303 and the deficit on the Center's Working Capital Fund decreased slightly by \$41,659 to \$363,606, trust fund income increased substantially by \$678,513 or 70 percent. This arises because of the ongoing initiative on nutrition and HIV/AIDS in the Caribbean and seven new projects, including supporting the development of a protocol for nutritional management of diabetes.
10. Expenditure administered by PAHO for the three sub-regional Centres, INCAP, CAREC and CFNI, increased from \$17,749,027 (2.4 percent of total expenditure) in 2002-2003 to \$20,258,533 (2.5 percent of total expenditure) in 2004-2005.
11. The timely payment of assessments is important to the ability of CFNI and CAREC to implement their programmes effectively and I would encourage Member States to adhere to the due times for payment of their contributions.
12. I have issued a separate audit opinion and report in relation to the Institute of Nutrition of Central America and Panama, INCAP.

ON FINANCIAL CONTROL IN THE FIELD

13. During 2004-2005, my staff carried out audit visits to PAHO Headquarters and six country offices (Paraguay, Colombia, Nicaragua, Venezuela, Cuba and Guatemala), as well as to the three sub-regional centres (INCAP, CAREC and CFNI) and three of the regional centres (CEPIS, INPPAZ and CLAP), to review local controls and the oversight provided by Headquarters, and to perform substantive testing.
14. Generally they found a high standard of financial control in operation. However, areas where improvements could be made were notified to the Organization and field offices by way of management letters containing observations and recommendations in respect of each visit.
15. In addition, while my staff were in Lima to visit the CEPIS office, they took the opportunity to revisit the Peru country office, previously visited in 2003, to confirm action taken on earlier audit recommendations. My staff were pleased to note that the recommendations had been acted on and were being implemented.

ON GOVERNANCE MATTERS

16. Sound governance arrangements are necessary to support effective financial management, accountability and proper stewardship of funds. As part of their audit for 2004-2005, my staff considered five key components of good governance arrangements, in addition to the importance of the accuracy and timeliness of financial statements on which I have previously commented:

- The assurance provided by internal oversight;
- The potential benefits of an audit committee;
- The arrangements for assessing and managing operational risks;
- The adequacy of the framework for expected ethical conduct; and
- Financial reporting standards.

Internal oversight

17. An agreement between WHO and PAHO signed in January 2004 stipulates that the internal audit team based in Washington will be dedicated to a consolidated internal audit of AMRO (the Regional Office of the Americas for WHO) and PAHO. However, internal oversight was under-resourced for the majority of the biennium and at the start of 2006 both internal oversight posts at PAHO Headquarters in Washington had become vacant.

18. Given the geographical and functional diversity of PAHO, a fully staffed internal oversight department with clear reporting lines is essential to the sound governance of the Organization. The fact that such a large proportion of the planned work was not completed during the biennium and that both posts are now vacant is of increasing concern. This is being addressed by management and I urge that action to reinstate an adequate level of internal audit oversight should continue to be treated as a matter of priority.

Audit committee

19. PAHO do not at present have an independent Audit Committee, and therefore lack the important oversight and independent advice which such a body would provide. Audit committees are a well-established and commonly accepted element of good governance arrangements; and the United Nations is now taking steps to improve its governance arrangements through the establishment of an independent oversight advisory committee. I have recommended that PAHO should similarly consider creating an independent oversight advisory committee and my report identifies ways in which the operation of such an audit committee might be developed.

Improved risk management

20. PAHO lacks a comprehensive and systematic approach to the management of risk at the strategic level. To help facilitate management in their responsibilities on internal control and governance, I have made recommendations on improved risk management. A formal risk management process is a valuable part of

sound management and can be used to provide assurance to Member States that PAHO management are effectively considering and managing organizational risk.

Ethics and Conduct

21. I made a number of observations and recommendations on the Organization's ethical framework and the introduction of a code of conduct in my biennial report for 2002-2003; my special report of 2004; and my follow up report of 2005. My staff have reviewed progress made in this area and further comments are set out in the section of this present report dealing with follow-up to previous recommendations.

Financial reporting standards

22. The effectiveness and integrity of financial reporting, and therefore accountability, is an important element in good governance. In November 2005, the Secretary-General's High Level Committee on Management took a decision to adopt the International Public Sector Accounting Standards (IPSAS) for the preparation of United Nations financial statements from 2010, subject to General Assembly approval in June 2006. This will result in improved, more complete, more transparent, more consistent and more useful financial reporting to Member States. The financial reporting requirements set out by the IPSAS are more stringent than those of the United Nations System Accounting Standards (UNSAS). PAHO will wish to consider the adoption of IPSAS to remain consistent with the rest of the UN system; and I have recommended that that PAHO prepares a detailed strategy and work plan for a move to IPSAS in 2010.

TRANSFER OF MAINFRAME OPERATIONS TO THE INTERNATIONAL COMPUTING CENTRE IN GENEVA

23. During the biennium, PAHO moved its mainframe computing operations from the Washington, D.C. Headquarters to the International Computing Centre (ICC) in Geneva. My staff reviewed the procedures involved in selecting ICC, transferring data from the mainframe to ICC, and user acceptance testing of ICC. I am pleased to report that procedures in selecting ICC were properly followed and that data transfer was validated to ensure that there was no loss or corruption of financial information.

FOLLOW-UP TO PREVIOUS AUDIT RECOMMENDATIONS

24. I made some 16 recommendations in the special report issued in September 2004 relating to PAHO's activities where they fell below best practice in terms of governance, and observations on management's progress in these areas are set out below in the Detailed Findings section of this present report.

25. Overall PAHO have made sound progress with implementing my recommendations in most areas. However, I note that both posts in the Internal Oversight Service became vacant at the start of 2006 and there is at present no oversight activity planned for 2006-2007. This is a serious cause for concern and I have made further recommendations on rectifying this situation.

26. The Executive Committee made recommendations relating to the appointment of an independent ombudsperson. With effect from 30 March 2006, Mr Wallace Meissner has been appointed as Ombudsperson, following open competition for the post.

DETAILED FINDINGS

OVERALL FINANCIAL POSITION OF THE ORGANIZATION

Budgetary Transfers and Program Delivery

27. Statement IV of the Financial Statements shows that the Organization obligated \$247,797,593 (95 percent) of the available appropriations from the 2004-2005 Effective Working Budget of \$259,530,000. This has been the first biennium in which the Effective Working Budget has included the \$72,730,000 WHO Regular Budget Allocation.

Results of the PAHO Regular Budget

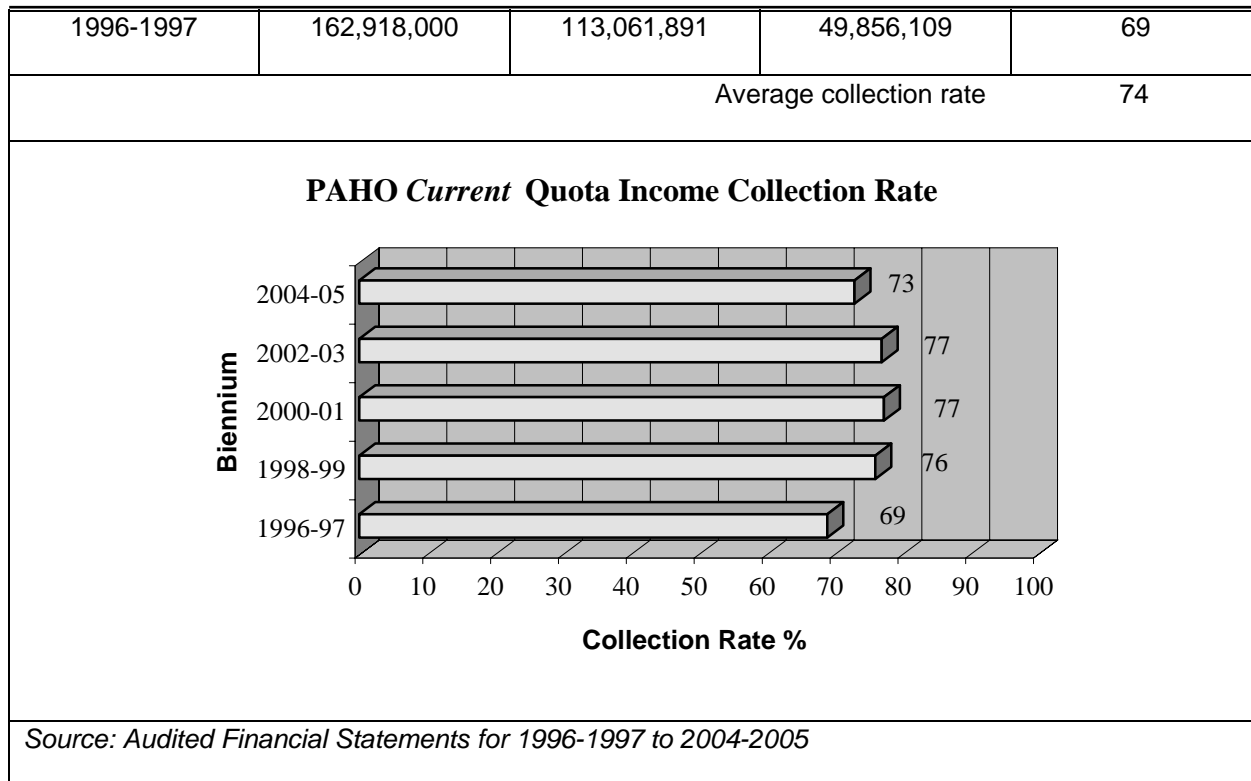
28. As shown in Statement I, in 2004-2005 the Organization received Regular Budget income of \$183,635,822, and incurred expenditure of \$175,259,824. After providing for delays in the collection of assessed contributions, and adjusting for contributions received in relation to prior periods and for savings on prior periods' obligations and other project adjustments, the excess of income over expenditure was \$5,998,568.
29. The 2004-2005 excess of \$5,998,568 compares with \$15,634 in 2002-2003, and this increase is due to an improvement in the collection of quota arrears (Figure 2 refers). Following a transfer of \$3,400,000 to Special Funds (Statement I.1), the overall increase in PAHO Regular Budget and Working Capital Fund for the biennium was \$2,598,568.

Quota Contributions

30. Figure 1 shows that for 2004-2005 PAHO achieved a collection rate for quota contributions due that was lower than the previous biennium at 73 percent, and lower than the average for the last 10 years.

FIGURE 1: THE COLLECTION RATE FOR CURRENT PAHO QUOTA CONTRIBUTIONS (excluding arrears)

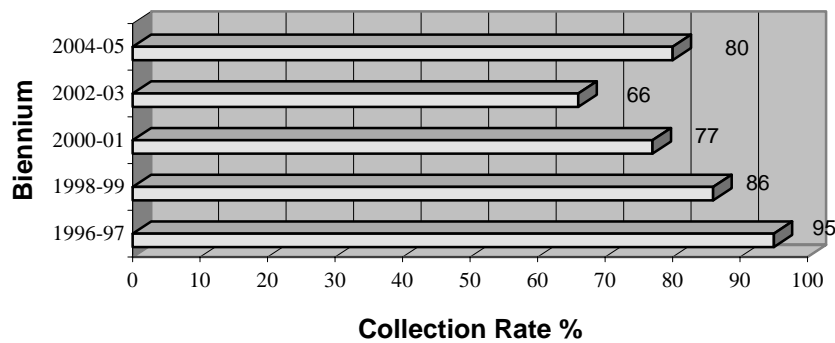
Biennium	Net Assessments	Amount Collected	Outstanding Contributions	Collection Rate
	\$	\$	\$	%
2004-2005	184,306,000	134,134,974	50,171,026	73
2002-2003	180,960,000	139,546,733	41,413,267	77
2000-2001	170,796,000	132,108,444	38,687,556	77
1998-1999	163,618,000	124,459,109	39,158,891	76



31. The Organization applies receipts from Member States to the oldest outstanding contribution. Figure 2 shows amounts received of \$46,628,436 in relation to contributions outstanding at 31 December 2003, representing a collection rate of 80 percent. This is higher than in 2002-2003 and marginally below the average for the last ten years. Of the \$61,740,124 outstanding at 31 December 2005 on quota assessments for the current and prior periods, \$15.6 million (25 percent) had been received by 31 March 2006.

FIGURE 2: COLLECTION RATE FOR ARREARS OF PAHO QUOTA CONTRIBUTIONS				
Biennium	Arrears	Payments received	Balance due 31 December	Collection Rate
	\$	\$	\$	%
2004-2005	58,197,534	46,628,436	11,569,098	80
2002-2003	49,216,339	32,432,072	16,784,267	66
2000-2001	46,596,506	36,067,723	10,528,783	77
1998-1999	52,128,026	44,690,411	7,437,615	86
1996-1997	49,204,772	46,932,855	2,271,917	95
Average collection rate				81

PAHO Quota *Arrears* Collection Rate



Source: Audited Financial Statements 1996-1997 to 2004-2005

Working Capital Fund

32. The Working Capital Fund stood at \$11,608,634 at 1 January 2004, comprising an unencumbered balance of \$9,018,643 and \$2,589,991 allocated for guarantee of loan. Despite a transfer to the Capital Equipment Fund of \$3,400,000, the overall balance increased to \$14,207,202 at 31 December 2005 due to the surplus from the 2004-2005 biennium. This is within the \$20,000,000 authorized for the Working Capital Fund by the 44th Directing Council in 2003-2004.

Trust Funds

33. Schedule 4 to the Financial Statements reports PAHO trust fund activity for the biennium. PAHO administered more than 450 trust fund projects during 2004-2005. Funds received increased by 24 percent to \$137,090,201 in 2004-2005, compared to \$110,549,418 in 2002-2003, while expenditure increased from \$107,158,512 in 2002-2003 to \$134,329,239 in 2004-2005. Trust Fund income represents donations made for specific projects by the donor; and the increase in income and expenditure reflects PAHO's success in attracting additional donations.

Special Funds

34. Statement I.1 of the Financial Statements reports an increase in income from \$20,452,451 to \$30,196,732 for the biennium; and an increase in expenditure from \$26,834,370 to \$31,074,453, mostly attributable to additional expenditure of some \$6 million on Natural Disaster Relief.

Non-Project Funds

35. Statement I.2 of the Financial Statements reports income of \$358,190,598, a decrease from \$363,315,599 in the prior biennium. Expenditure rose from \$334,758,502 in 2002-2003 to \$356,627,962 in 2004-2005. Essentially this was due to the increased activity of the Revolving Fund for the Expanded Program on Immunization, which rose from \$289,783,443 in 2002-2003 to \$314,165,224. Details are reported in Schedule 3 to the Financial Statements.

WHO Funds

36. PAHO acts as the Regional Office of the Americas for WHO, AMRO, and administers WHO activities in the Americas. Statement I of the Financial Statements shows that the WHO Regular Budget fell by 1 percent, from \$73,247,611 in 2002-2003 to \$72,537,769 in 2004-2005. Statement I.4 shows a significant increase in WHO Other (non-Regular Budget) Funds of 83 percent, from \$13,282,898 in 2002-2003 to \$24,349,304 in 2004-2005. This increase was due to additional funding of Voluntary Funds for Health Promotion and specifically for the HIV/AIDS, TB and Malaria fund.

Total Funds

37. Total PAHO expenditure across all funds increased by 10 percent from \$717,888,896 in 2002-2003 to \$786,316,900 in 2004-2005 (after eliminations). This increase reflects the increased activity of the Trust Funds, the Expanded Program on Immunization, and WHO Other Funds as described above. Total fund balances increased by \$9,714,508 during the biennium and although the collection of prior years' assessed contributions increased by \$14,196,364 compared to the previous biennium, net cash and term deposits decreased by \$37,494,781. This reflects a \$25,520,507 increase in investments, excess income over expenditure of \$8,279,285 (excluding the regional centres) and a net decrease in balance payable to the World Health Organization of \$22,603,933.

Transfers between Funds

38. During 2004-2005 only one transfer was made between PAHO's different funds, of \$3,400,000 from the Working Capital Fund to the Capital Equipment Fund for the future purchase of computer equipment.

Eliminations for intra-group transactions on all Funds

39. In the 2002-2003 Financial Statements, PAHO introduced the additional disclosure of eliminations, where transactions between funds were eliminated to avoid double counting. My staff conducted further work during 2004-2005 and identified some \$15.3 million eliminations relating to the 2002-2003 biennium in addition to the \$10.9 million already identified during the previous period. These concern intra-fund transactions and eliminations from INCAP and CAREC which had previously not been included. The amounts identified are material to the accounts and PAHO have re-stated the 2002-2003 comparative figures disclosed in the biennial financial statements for 2004-2005.

40. Eliminations of \$28.1 million have been made for 2004-2005 and these relate to transactions between funds and within funds for each organisation as follows:

- PAHO - \$25.6 million;
- INCAP - \$1.4 million; and
- CAREC - \$1.1 million.

Cases of fraud and presumed fraud

41. The Organization has informed me that there were ten cases of fraud detected during the biennium. Of \$83,225 misappropriated, all but \$24 was recovered prior to 31 December 2005.

Other losses and amounts written off

42. The Organization has notified me of the write-off of uncollectible receivables amounting to \$5,227 and a total of administrative waivers of \$366,432. Details are given in Note 25 to the financial statements.

Ex-gratia payments

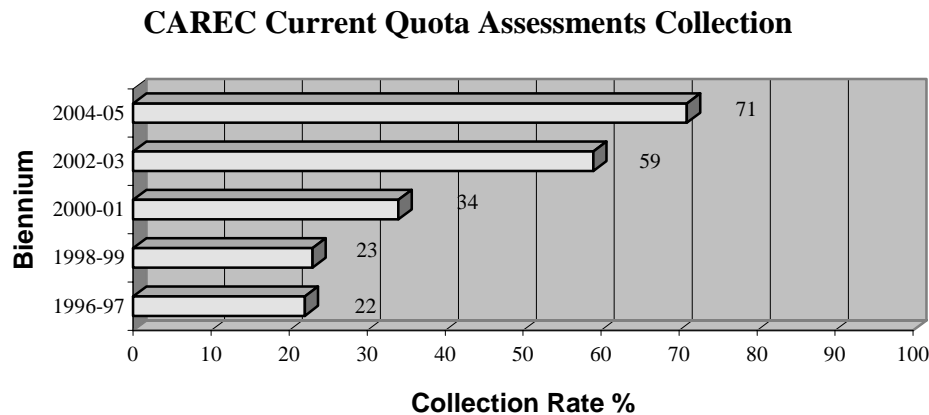
43. The Organization also stated that ex-gratia payments of \$6,552 were made during 2004-2005.

FINANCIAL POSITION OF THE CENTRES**Caribbean Epidemiology Center (CAREC)****Quota Contributions**

44. Figure 3 shows that CAREC's collection rate of current assessments rose to 71 percent in 2004-2005, the best current collection rate for some years. At 71 percent, the collection rate is only slightly lower than the comparable rate for PAHO (73 percent).

FIGURE 3: COLLECTION RATE FOR CURRENT CAREC QUOTA CONTRIBUTIONS (excluding arrears)

Biennium	Net Assessments	Amount Collected	Outstanding Collection	Collection Rate
	\$	\$	\$	%
2004-2005	4,308,852	3,044,002	1,264,850	71
2002-2003	3,849,202	2,289,685	1,559,517	59
2000-2001	3,599,228	1,208,442	2,390,786	34
1998-1999	3,410,400	800,474	2,609,926	23
1996-1997	3,360,000	738,515	2,621,485	22
Average collection rate				42



Source: Audited Financial Statements 1996-1997 to 2004-2005

45. CAREC also collected \$759,310 of total prior period assessments amounting to \$3,820,911 in 2004-2005: 20 percent of amounts in arrears compared to 47 percent in 2002-2003. As a result of the lower collection rate for prior year assessments, total contributions outstanding increased from \$3,820,911 at the end of 2003 to \$4,326,451 at 31 December 2005. Of the balance owing at 31 December 2005, 85 percent was due from just two Member States. Neither country has made any payment for more than 8 years.
46. My staff noted the continued efforts made by CAREC to encourage Member States to pay their assessments. Nevertheless, the continued arrears impair the Center's ability to plan and carry out its activities and could place at risk its continued financial viability.

Overall Financial Position

47. CAREC's Regular Budget income rose from \$3,941,739 in 2002-2003 to \$4,404,936 in 2004-2005, largely due to an increase in quota contributions. Regular Budget expenditure also rose, from \$3,796,159 in 2002-2003 to \$4,197,126 in 2004-2005. After other adjustments and a provision for delays in the collection of assessed contributions, the deficit for 2004-2005 was \$273,158, thereby decreasing the balance on the Working Capital Fund to \$672,687 as at 31 December 2005.
48. CAREC recorded a fall in Trust Fund income from \$6,998,770 in 2002-2003 to \$6,344,584 in 2004-2005. However, this is still above the level of \$4,025,090 received in 2000-2001. There were eleven new Trust Funds in 2004-2005, which collectively generated income of \$2,424,553 during the period; the majority of these receipts related to activities on HIV/AIDS prevention and control.
49. CAREC's funding from PAHO rose from \$1,968,825 in 2002-2003 to \$2,503,348 in 2004-2005. In addition, CAREC received direct funding from WHO in 2004-2005 of \$22,600. Total fund balances rose by \$528,787 over the biennium, to \$5,202,756 at 31 December 2005. This represents an increase of 11 percent.

Caribbean Food and Nutrition Institute (CFNI)

Quota Contributions

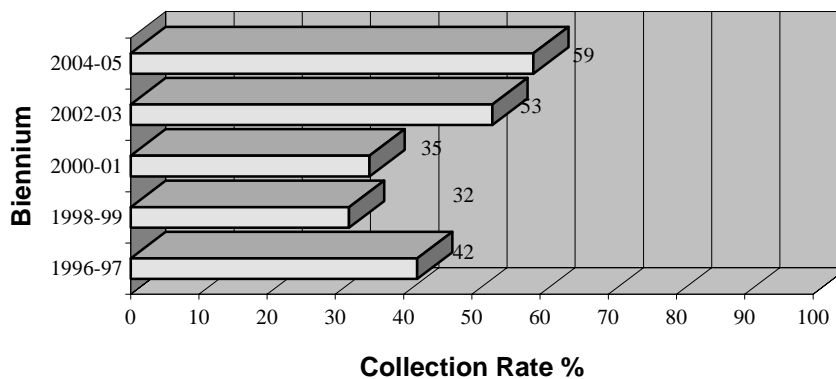
50. Figure 4 shows that during 2004-2005 the amount collected on current assessments was higher than in 2002-2003. However, the collection rate for 2004-2005 at 59 percent remained significantly lower than the comparable rate for PAHO and CAREC.

FIGURE 4: COLLECTION RATE FOR CURRENT CFNI QUOTA CONTRIBUTIONS

(excluding arrears)

Biennium	Net Assessments	Amount Collected	Outstanding Collection	Collection Rate
	\$	\$	\$	%
2004-2005	712,268	423,043	289,225	59
2002-2003	688,969	367,937	321,032	53
2000-2001	665,670	233,296	432,374	35
1998-1999	649,825	207,171	442,654	32
1996-1997	633,980	263,777	370,203	42
Average collection rate				44

CFNI Current Quota Assessments Collection Rate



Source: Audited Financial Statements 1996-1997 to 2004-2005

51. In addition to the improved collection of current period assessments, CFNI also collected marginally higher amounts in relation to prior years, at \$199,944 compared to \$174,344 in 2002-2003. However, this is still significantly below the collection of \$457,197 in 2000-2001. Total outstanding contributions rose to \$1,391,292. Of this amount, the host country owes \$1,362,943, or 98 percent.

52. During their audit, my staff noted the efforts made by the Institute to encourage Member States to pay their assessments. Nevertheless, continued arrears impair CFNI's ability to plan and carry out activities, and could place at risk its continued financial viability. I therefore continue to encourage Member States to adhere to the due times for payment of their contributions.

Overall Financial Position

53. CFNI's Regular Budget income rose from \$688,969 in 2002-2003 to \$712,268 due to increased assessed quota contributions, while Regular Budget expenditure fell slightly from \$603,878 in 2002-2003 to \$581,328 in 2004-2005. After adjustments for delays in the collection of quota income, CFNI recorded a surplus of \$41,659 for 2004-2005, thereby decreasing the deficit balance of the Working Capital Fund to \$363,606.
54. There has been a continued increase in CFNI Trust Fund activity during the period. Most of the ten existing Trust Fund projects finished during the biennium, and CFNI replaced these with seven new ones. Trust Fund income, which had been just \$346,306 in 2000-2001 and \$972,144 in 2002-2003, rose to \$1,650,657 in 2004-2005. The increase was chiefly due to a continuing project on nutrition and HIV/AIDS in the Caribbean, and a new project focusing on tackling diabetes in the region.
55. CFNI's funding from PAHO increased from \$1,812,241 in 2002-2003 to \$1,822,119 in 2004-2005, with a similar increase in funding from WHO, rising from \$605,775 in 2002-2003 to \$749,496 in 2004-2005.
56. In my 2000-2001 and 2002-2003 reports, I recommended that PAHO and CFNI should continue to keep the Institute's financial position under review. Despite the continued increase in trust fund activities in 2004-2005, with a continuing deficit on the Working Capital Fund and reliance on advances from PAHO and WHO (albeit reduced), CFNI's financial position should remain under review.

FINANCIAL CONTROL IN THE FIELD

Regional centres

57. In addition to the sub-regional centres (INCAP, on which I provide a separate audit opinion and report, CAREC and CFNI), PAHO administers a number of regional centres:
- BIREME – the Latin American and Caribbean Center on Health Sciences Information;
 - CEPIS – the Pan American Center for Sanitary Engineering and Environmental Sciences;
 - CLAP – the Latin American Center for Perinatology and Human Development;
 - INPPAZ – the Pan American Institute for Food Protection and Zoonoses;
 - PANAFTOSA – the Pan American Foot-and-Mouth Disease Center.
58. In September 2005, under Resolution CD46.R6, the Directing Council requested that the Director disestablish the Pan American Institute for Food Protection and Zoonoses (INPPAZ) in order to re-engineer PAHO's technical co-operation strategy in support of food safety. This was driven by the availability of institutions of excellence and networks developed in the region to deal with food safety. The Council

consider there is no longer a need for a specialized Pan American centre with the characteristics of INPPAZ. The disestablishment of INPPAZ is expected to generate savings of some \$600,000 a year, which can be used on food safety technical co-operation within the emerging centres of excellence in the region.

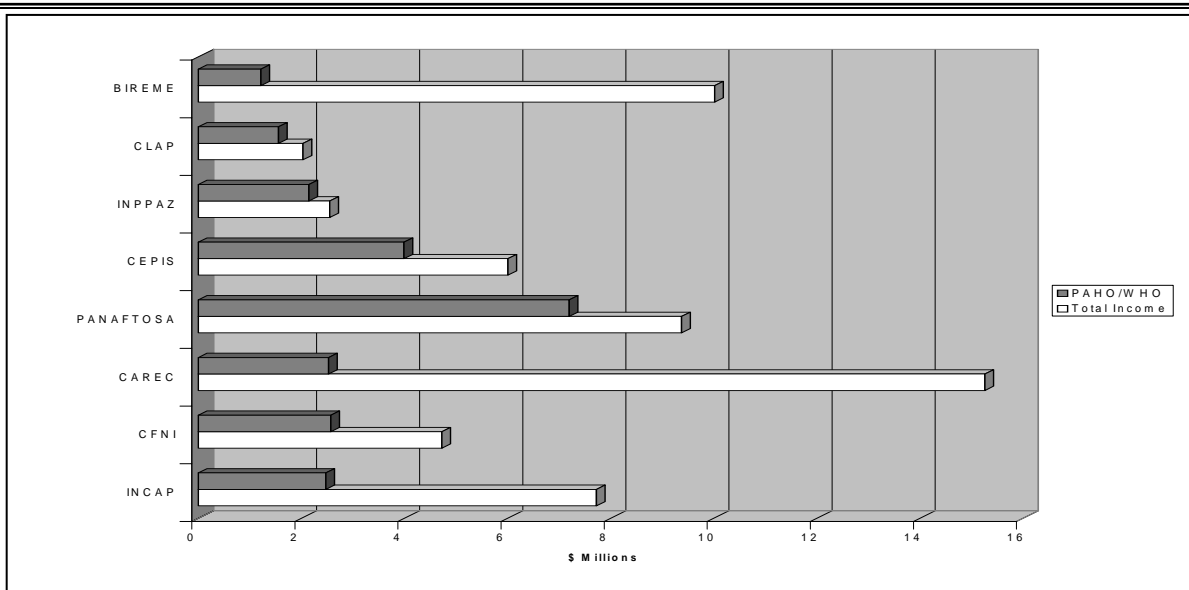
PAHO's Regular Budget financing of the centres

59. PAHO finances the regional and sub-regional centres in various ways. It may provide funding through its own Regular Budget, through the WHO Regular Budget, or by means of transfers from other funds, for example special funds. Figure 6 shows the extent to which PAHO/WHO finance the centres.

60. In 2004-2005, PAHO increased its support to the five regional centres by some \$0.5 million. In particular, the Organization increased support for INPPAZ from \$2,505,318 to \$3,184,884. Nevertheless, as Figure 6 shows, the eight centres continue to require a high proportion of overall support from PAHO.

FIGURE 6: PAHO/WHO FINANCING OF CENTRES

Centre	PAHO/WHO Financing 2004-2005 \$	Total Income 2004-2005 \$	%
Regional Centres			
BIREME	1,217,153	10,017,868	12
CLAP	1,554,976	2,034,054	76
INPPAZ	2,144,994	2,549,099	84
CEPIS	3,990,703	6,007,359	66
PANAFTOSA	7,194,570	9,376,545	77
Sub-Regional Centres			
CAREC	2,525,948	15,259,341	17
CFNI	2,571,615	4,724,221	54
INCAP	2,474,864	7,724,053	32
Total	23,674,823	57,692,540	41



Source: PAHO/INCAP accounting records

External Audit visits to PAHO Headquarters and field offices

61. During 2004-2005, my staff carried out audit visits to PAHO Headquarters and six country offices: Paraguay, Colombia, Nicaragua, Venezuela, Cuba and Guatemala. They also visited the three sub-regional centres at CAREC, CFNI, INCAP; and the three regional centres, CEPIS, INPPAZ and CLAP.
62. The audit work undertaken at each office included a review of financial controls, to ensure that they were adequate and consistent with Headquarters' requirements; and testing to verify the operation of those controls. In addition to reviewing controls, my staff tested a number of transactions to ensure that income and expenditure has been properly brought to account. The results of this examination indicated that in general there was a high standard of financial control exercised at the field offices, supplemented by a satisfactory level of oversight from Headquarters. Overall, this indicated a sound level of assurance that expenditure at the field offices and Headquarters was accurately and properly recorded, and accounted for in line with the Organization's aims and objectives.
63. Detailed findings from the audit visits were notified to the Organization and field offices in management letters; and action is being taken on the recommendations made. Audit recommendations were all in respect of improving existing controls - principally in the following four areas: reconciliation of local income; supporting documentation on payments; monitoring of expenditure (including projects, general expenditure and monthly payroll costs); and fixed asset management. These findings are similar to those identified during the 2002-2003 biennium and it would appear that these previous recommendations are not being shared with sufficient emphasis to lead to their implementation in all field offices.
64. In addition to the visits referred to above, while my staff were in Lima to visit the CEPIS office, they took the opportunity to revisit the Peru country office, previously visited in 2003, to confirm that action had been taken in relation to the audit recommendations. My staff were pleased to note that the recommendations had, indeed, been acted upon and were being implemented.

GOVERNANCE MATTERS

Internal Oversight

65. Good governance requires the maintenance of an adequate system of internal control; and the internal audit function is a vital source of assurance for management and the governing bodies over the effectiveness of that internal control environment. PAHO's Internal Oversight has been under-resourced for the majority of the biennium resulting in the postponement or cancellation of 20 of the 36 planned reports. An agreement between WHO and PAHO signed in January 2004 stipulates that the internal audit team based in Washington will be dedicated to a consolidated internal audit of AMRO (the Regional Office of the Americas for WHO) and PAHO. However, at the start of 2006 both Internal Oversight posts at PAHO Headquarters in Washington had become vacant.
66. Given the geographical and functional diversity of PAHO, a fully staffed internal oversight department with clear reporting lines is essential to the sound governance of the Organization. The fact that such a large proportion of the planned work was not completed during the biennium and that both posts are now vacant is of increasing concern, although management are aware of these problems and, in conjunction with the WHO Internal Oversight service, are taking steps to fill vacancies and ensure improved internal audit coverage for the future.

Audit Committee

67. The Director of PAHO carries responsibility and accountability to the governing bodies for the system of internal control and the management of risk within the Organization. Audit committees are a well-established and commonly accepted element of good governance arrangements; and an effective and challenging audit committee can be a prime source of assurance for the Director in discharging these responsibilities. PAHO does not have an audit committee at present.
68. The United Nations is now taking steps to improve its governance arrangements through the establishment of an independent oversight advisory committee and has articulated a good practice framework for the implementation and independence of an audit committee, on which PAHO could model an equivalent development.
69. If these arrangements operate effectively, they offer an increased level of assurance to Member States on the satisfactory maintenance of internal controls, reinforce the work of both internal and external auditors and hence lead to an improved quality of governance, through the audit committee:
- Reviewing and monitoring the adequacy, efficiency and effectiveness of the Organization's system of internal controls and risk management;
 - Reviewing and ensuring implementation of internal and external audit recommendations;
 - Reviewing the work plan of internal audit;

- Monitoring and reviewing the effectiveness of the Organization's internal audit function; and
- Providing a forum to monitor and review the engagement of the External Auditor.

Recommendation 1: *I recommend that PAHO consider the creation of an Audit Committee, preferably to be chaired by an independent non-executive member and with a majority of external members.*

Improved Risk Management

70. The effective management of operational or business risks is an important element of modern good governance practice, to support the achievement of an organization's objectives at an acceptable cost. While staff may manage risk intuitively in the course of their duties, PAHO does not have any framework for the systematic identification, assessment and management of operational and corporate risks at a strategic level. For example, PAHO does not maintain a risk register recording key risks to the Organization and demonstrating how these risks are assessed, monitored and managed.

Recommendation 2: *I recommend that the Director of PAHO should consider introducing a systematic process of identifying, measuring and managing corporate risks. Such risks should be recorded in a risk register which is regularly reviewed and updated to ensure that key corporate risks are being managed effectively.*

Ethics and Conduct

71. The proper conduct of the Organization's business, and the ethical framework against which operational activities are carried out, is fundamental to good governance. I made a number of observations and recommendations concerning the Organization's ethical framework, including the introduction of a code of conduct, in my biennial report for 2002-2003, my special report of 2004 and follow up report of 2005. Detailed comments on progress in this area are set out below in the section of this present report dealing with follow-up to previous recommendations.

Financial Reporting Standards

72. PAHO's financial statements are prepared in accordance with the United Nations System Accounting Standards (UNSAS). In November 2005, the Secretary-General's High Level Committee on Management

took a decision to adopt the International Public Sector Accounting Standards (IPSAS) for the preparation of United Nations financial statements from 2010, subject to the General Assembly approval in June 2006.

The financial reporting requirements set out by the IPSAS are more stringent than those of UNSAS.

73. The adoption of and adherence by United Nations entities to an independent, recognised and commonly-accepted accounting framework is a beneficial and welcome development. Compliance with independent international standards will ensure improved comparability between the finances and financial results of entities in the UN system; and lead to more consistent, better understood and more informative financial reporting. Compliance in the UN with independent and generally-accepted accounting practice and reporting standards will contribute to the visible demonstration of high standards of financial management; and will enhance transparency, accountability and governance.
74. The United Nations Task Force on Accounting Standards, on which the UN entities, the Specialized Agencies and the International Atomic Energy Agency are represented, has recognised that the adoption of IPSAS will also bring the benefits of improved financial information, supporting better financial management, improved results-based management where applicable, and better quality and credibility for UN System financial reports.
75. The external auditors of the UN System, including the United Kingdom National Audit Office, are keen to support organisations in the transition to IPSAS, and to provide advice and support consistent with the External Auditor's independent oversight role.
76. Compliance with International Public Sector Accounting Standards will involve, amongst other things, annual financial reporting where organisations have previously produced audited accounts on a biennial basis. This more frequent reporting will itself improve accountability and governance by providing authoritative results more promptly to support financial management and decision making. Member States will have the advantage of receiving financial and audit reporting earlier and more frequently; and thus be able to act more quickly to improve systems and controls, or to manage risk and save money.
77. PAHO will wish to consider the adoption of IPSAS in keeping with the rest of the United Nations system; and should consider developing an appropriate project plan and assess the requirements and resources which will be needed, particularly in relation to knowledge, skills, information technology and training as appropriate.

Recommendation 3: I commend the adoption of the independent IPSAS accounting standards to PAHO as an appropriate financial reporting framework and recommend that the Organization prepares a detailed strategy to provide for this development.

TRANSFER OF MAINFRAME OPERATIONS TO THE INTERNATIONAL COMPUTING CENTRE IN GENEVA

78. In 2004-2005 PAHO moved its mainframe computer from its Washington, D.C. Headquarters to the International Computer Centre (ICC) in Geneva. PAHO conducted a feasibility study in December 2003 and identified that the key objective for the transfer was to reduce the running costs of mainframe operations. The contract for outsourcing mainframe operations was awarded to ICC following a competitive bidding process where ten bids were invited and four bids were received. The ICC offered a combination of greater technical expertise and lower cost than other bidders. I am satisfied that appropriate procedures were followed in awarding ICC the contract for running PAHO's mainframe operations.
79. PAHO's mainframe computer processed not just financial data but also other operational information such as personnel data. It was vital for the operational continuity that the transfer of processing from the mainframe computer was planned and managed effectively to ensure that no data was lost or corrupted.
80. PAHO produced a detailed acceptance testing plan setting out the procedures to be followed for data transfer, validation of migrated data and user acceptance of new functionality. My staff reviewed the arrangements and are satisfied that appropriate procedures were followed to transfer information ensuring that such data was complete and uncorrupted.
81. PAHO used the test environment on their existing mainframe to upload all existing data using back ups of live data. The data uploaded into the test environment was then transferred on to the ICC system and reports were produced on all key aspects of finance (such as the trial balance, budgetary report and statement of trust funds) from both the existing and new systems, with cross-checking to ensure a successful transfer had been achieved.
82. In order to be satisfied that data had been properly transferred from PAHO's previous system to the ICC, my staff reviewed the transfer process. This involved reviewing the planning process and the testing carried out by PAHO IT staff on the accurate migration of data from their existing system to ICC. My staff obtained assurance that data migration from the old system to the new was properly managed by interviewing key personnel involved in data transfer; and by re-performing checks on reports produced from PAHO's old mainframe system and ICC to confirm that both report totals and the value of underlying transactions agreed.
83. My staff were satisfied therefore that PAHO took appropriate steps to:
- Select a contractor to outsource their mainframe operations using competitive tendering;
 - Plan the transfer of data from their existing mainframe system to the ICC operation;
 - Validate that data transferred was complete and accurate; and
 - Carry out follow up work to ensure data integrity.

FOLLOW-UP TO PREVIOUS AUDIT RECOMMENDATIONS

84. In my report on the 2002-2003 audit, and my special report and follow-up report issued to the Directing Council in September 2004 and September 2005 respectively, I highlighted several areas where governance procedures at PAHO fell below best practice. In addition to the two recommendations made by the Executive Committee, I made sixteen recommendations on areas for improvement under the following headings:

- Ethical standards and code of conduct;
- Recruitment of employees and consultants;
- Complaints procedures, investigation and reporting;
- Management of external relationships;
- IT security;
- Internal audit; and
- Independence of the Ombudsman.

85. My staff followed up these matters as part of their 2004-2005 end-of-biennium audit and I am able to report that a significant amount of progress has been made on implementing these recommendations. PAHO have:

- Implemented a new Code of Ethical Principles and Conduct from 1 January 2006;
- Required all staff to make a declaration of interests;
- Appointed an ombudsperson with effect from 30 March 2006; and
- Made progress with developing the Integrity and Conflict Management System expected to be fully operational by May 2006.

86. However, as I have already noted above, the Internal Oversight Service is significantly understaffed and further progress needs to be made to achieve an acceptable level of oversight coverage and assurance. I also note that the post of Ethics Officer remains vacant, although PAHO are actively working to fill this.

Ethical Standards and Code of Conduct

87. PAHO have developed a new Code of Ethical Principles and Conduct which was presented to the Directing Council during their 46th meeting in September 2005 as an information document. The Code of Ethical Principles and Conduct has been implemented from 1 January 2006 and applies to all staff who work for PAHO regardless of the type of appointment held or the duration of appointment. The Code has been widely disseminated throughout PAHO and staff must submit annually a Statement of Acknowledgement, contained in the Code to Human Resources Management. PAHO are developing and finalizing training courses for staff with a view to providing training in April and May 2006.

88. I also recommended that PAHO staff in sensitive posts, such as senior management positions, procurement and human resources, should complete a comprehensive declaration of interests on a regular basis. PAHO

adopted the World Health Organization (WHO) form for declaring interests and expanded this to include a wider definition of related parties, including immediate family members. All relevant staff were sent a PAHO Declaration of Interest Disclosure Program notification and appropriate forms on 17 August 2005 and by March 2006 some 95 percent of returns had been received. The Legal Services team are pursuing outstanding returns.

89. In pursuance of making the Code of Conduct and declaration of interest more effective, I recommended that there should be transparent procedures for the investigation of any breaches of the Code or the failure to properly disclose interests. PAHO are undertaking the appointment of an Ethics Officer who would have responsibility for monitoring compliance with the Code of Conduct and any failure to declare interests. As at 31 March 2006, the Ethics Officer was yet to be appointed.

Recruitment of employees and consultants

90. Following a review of recruitment procedures for employees and consultants, I recommended that PAHO maintain an up to date list of accredited Short Term Consultants (STCs) and Short Term Professionals (STPs). PAHO have engaged a company with expertise in preparing automated rosters for medical professionals to develop a suitable system for maintaining a record of accredited STCs and STPs. The system is expected to be in place by August 2006. My staff will review progress on implementing this system during the 2006-2007 biennium.
91. I further recommended that all such STCs and STPs should be recruited on the basis of open competition in all but the most exceptional circumstances. Where candidates fill such posts on a temporary basis, they should be required to comply with the Code of Conduct. PAHO remain committed to ensuring rigorous competitive selection for temporary personnel. However, PAHO is engaged in discussions with the World Health Organization on contract reform where, for example, temporary staff engaged for a period of up to two years would no longer be considered to be short term contract staff. My staff will keep developments under review during the 2006-2007 biennium.
92. In terms of internal appointments I recommended that procedures for such appointments should be the same as those for external appointments. PAHO have now introduced equivalent procedures for internal appointments as for external appointments. PAHO are considering a proposal from their Recruitment Unit to provide greater transparency on internal selection procedures and standards. I welcome the progress made in this regard.

Complaints procedures, investigation and reporting

93. I recommended that, in line with best practice, PAHO should introduce a clear policy and procedure for dealing with complaints and allegations which can be disseminated to staff. Such procedures were required

to establish clear timeframes for investigating and communicating complaints and allegations. I further recommended that where normal line management channels have been exhausted or are not appropriate, a confidential hotline be set up for staff to air their concerns and grievances.

94. Since my report PAHO have been actively developing the Integrity and Conflict Management System (ICMS) with the following objectives:

- Comprehensive and integrated conflict management will be handled beyond case-by-case efforts;
- Systematic issues are recognized and addressed;
- Multiple options for staff will be available depending on the issues involved;
- Co-ordinated response is provided regardless of the chosen forum for pursuing complaints;
- More efficient use of resources; and
- An improved work environment.

95. ICMS is expected to be fully implemented by May 2006 and all complaints and allegations will be handled according to an established procedure. PAHO are also developing an Integrity Helpline which will be a confidential free telephone service for all staff. My staff will review the introduction of ICMS during the 2006-2007 Biennium.

96. To support my earlier recommendations, I also highlighted the need to have a clear policy in place setting out the criteria under which complaints would be investigated and personnel involved in the investigation. I note that in developing the ICMS, PAHO are establishing investigative protocols and procedures to handle complaints fairly and objectively. As noted earlier, PAHO are in the process of appointing an Ethics Officer who is charged with managing complaints through a three stage process covering:

- Intake and evaluation;
- Preliminary enquiry; and
- Detailed investigation.

97. My recommendations in this area were buttressed by the overall need for the Legal Department to be involved in all key stages of any investigation that is undertaken. PAHO have fully accepted and implemented this recommendation and the Legal Department are being fully integrated within ICMS.

Management of external relationships

98. Where PAHO enter into partnerships with third parties, I recommended that third party partners should conform to ethical standards set by PAHO for itself. To this end PAHO have developed guidelines to help evaluate the suitability of potential partners. These guidelines were reviewed and approved by the Director and presented at the 46th Session of the Directing Council in September 2005 as an information document.

99. I further recommended that PAHO should establish appropriate policies and guidelines to cover the management of relationships with third party organisations. These should be supported by Memoranda of Understanding in individual cases, to define the relationship, roles and responsibilities of the parties.
100. Additionally, in 2004 PAHO developed policies and procedures for reviewing all technical co-operation initiatives with third party organizations and donor countries. These procedures ensure that extra budgetary initiatives are coherent with the Organization's priorities and areas of work; that the proposed projects are technically sound and well designed; that project management is consistent with the Organization's rules and procedures; and that projects are financially self-reliant.
101. In accordance with the above referenced procedures, extra budgetary initiatives must be supported by Memoranda of Understanding (MoUs) or agreements defining the relationships and responsibilities of all parties. A MoU is now set up immediately when there are to be financial transactions between PAHO and another body.
102. I also recommended that PAHO should exert greater control over the use of its name and logo. I note that in accordance with the PAHO/WHO Manual, requests for permission for outside bodies to use PAHO's logo in ways other than on publications must be sent with full justification to PAHO's Legal Department. Where the Legal Department is aware of inappropriate use, it aims to move swiftly to rectify the matter. However, in the past not all incidences have been reported and new directives will be issued to remind all staff to be vigilant and report any incidences of inappropriate use to the Legal Department.
103. Directives regarding the use and control of the Organization's name and logo will be issued to all staff and will be included in the orientation seminars for new staff members. Additionally, the use of PAHO's name and logo as well as the "corporate identity system" will be reviewed as part of the initiatives under PAHO's Roadmap for Institutional Transformation.

IT Security

104. In my last report I recommended that PAHO should carry out a review of IT security arrangements, including those relating to e-mail facilities. In addition I recommended that PAHO should develop a detailed policy on IT security and take steps to ensure that it is actively enforced.
105. The Director of PAHO has created a post of Information Security Officer within the Administration Department. This post was filled with effect from 1 October 2005 and a detailed work plan has been developed and approved. The plan includes:
- The development and issuance of an IT security policy and security awareness program;
 - Monitoring of compliance with the security policy;
 - Disaster recovery planning; and

- Risk assessments and implementation of security measures in relation to IT.

Internal Oversight

106. In 2002-2003 I reported that internal audit had been under-resourced for the majority of the biennium and that the work programme had to be cut back. In September 2005 I further reported that, although PAHO's department of Internal Oversight Services (IOS) were fully staffed once again, there was nonetheless a need to review the IOS resources. However, I note that at the start of 2006 the Internal Oversight Service had lost both members of staff and no audit programme for the 2006-2007 biennium had been finalised.
107. My staff have discussed their concerns on the lack of internal oversight coverage for the current biennium with PAHO senior management and they were advised that, following a review of the role of internal oversight, it had been decided to create three positions. The relationship with the World Health Organization's internal oversight services was to be agreed with WHO in April 2006 and the three positions filled as soon as possible thereafter. The Director of PAHO is arranging for the WHO Internal Oversight team to assist with the oversight work plan for 2006 while these positions are being filled.

Independence of the Ombudsperson

108. The Executive Committee also called for there to be a report on the selection of an Ombudsperson. I note that the Director of PAHO has now appointed an Ombudsperson with effect from 30 March 2006. The Ombudsperson will be an essential component of the Integrity and Conflict Management System.

ACKNOWLEDGEMENT

109. I wish to record my appreciation for the willing co-operation and assistance extended by the Director and the officers of the Organization throughout the course of this audit.



Sir John Bourn

Comptroller and Auditor General, United Kingdom

External Auditor

AUDIT SCOPE AND APPROACH

Audit scope

The audit covers the examination of the Financial Statements of the Pan American Health Organization (PAHO) for the financial period ended 31 December 2005 in accordance with Regulation XIV of the Financial Regulations.

In accordance with the agreed arrangements, the External Auditor has provided a separate audit opinion and report on the Financial Statements of the Institute of Nutrition of Central America and Panama (INCAP) for the financial period ended 31 December 2005.

Audit Objectives

The main purpose of the audit was to enable us to form an opinion as to whether the expenditure recorded in the biennium had been incurred for the purposes approved by the PAHO governing bodies; whether income and expenditure were properly classified and recorded in accordance with the Financial Regulations; and whether the Financial Statements presented fairly the financial position as at 31 December 2005.

Audit Standards

Our audit of the Organization's 2004-2005 Financial Statements was carried out 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. These standards require us to plan the audit so as to obtain reasonable assurance that the Organization's Financial Statements are free of material misstatement. The Organization's management were responsible for preparing these Financial Statements, and we are responsible for expressing an opinion on the statements, based on evidence collected in the audit.

Audit Approach

In accordance with the Common Auditing Standards, our audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the Financial Statements. This included:

- a general review of the Organization's accounting procedures;
- a broad assessment of the internal controls for income and expenditure; bank accounts; accounts receivable and payable; and supplies and equipment;
- substantive testing of transactions of all types;

- substantive testing of year end balances; and
- a final examination to ensure that the Financial Statements accurately reflected the Organization's accounting records and were fairly presented.

These audit procedures are designed primarily for the purpose of forming an opinion on PAHO's Financial Statements. Consequently the work did not involve a detailed review of all aspects of financial and budgetary systems and the results should not therefore be regarded as a comprehensive statement on them.

Internal Audit

As in previous audits, we continued to liaise with the department of Internal Oversight Services on matters of joint interest. Where we consider that we can place reliance on the work of Internal Audit it is our practice to do so, particularly in circumstances where such reliance avoids unnecessary duplication of audit procedures.

Reporting

Observations on matters which we consider should be brought to the attention of the Directing Council are set out in this report. In accordance with normal professional audit practice, we also provide the Organization with management letters setting out the detailed findings arising from our examination.

Audit Results

During the audit, we sought explanations as we considered necessary in the circumstances on matters arising from the examination of the internal controls, accounting records and financial statements. None of these matters materially affected our audit opinion on the Organization's financial statements for the biennium and, notwithstanding the observations in this report, our examination revealed no weaknesses or errors that we considered material to the accuracy, completeness and validity of the financial statements as a whole. Accordingly the External Auditor has placed an unqualified opinion on the financial statements of the Organization for 2004-2005.

OPINION OF THE EXTERNAL AUDITOR

To: The Directing Council of the Pan American Health Organization

I have audited the accompanying financial statements, comprising Statement I to X, Schedules 1 to 8 and the supporting Notes to the Pan American Health Organization for the financial period ended 31 December 2005. These financial statements are the responsibility of the Director. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my 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 I 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, 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 Director, as well as evaluating the overall financial statement presentation. I believe that my audit provides a reasonable basis for the audit opinion.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Pan American Health Organization as at 31 December 2005 and the results of operations and cash flows for the period then ended in accordance with the United Nations System Accounting Standards and the Organization's stated accounting policies set out in Note 2 of the financial statements, which were applied on a basis consistent with that of the preceding financial period.

Further in my opinion, the transactions of the Pan American Health Organization, which I have tested as part of my audit, have in all significant respects been in accordance with the Financial Regulations and legislative authority.

In accordance with Article XIV of the Financial Regulations, I have also issued a long-form Report on my audit of the Pan American Health Organization's financial statements.



Sir John Bourn
Comptroller and Auditor General,
London, United Kingdom
External Auditor
 15 April 2006