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# INFORMATION NOTES

## REPORT OF THE EXTERNAL AUDITOR

### Review of Corporate Governance at the World Food Programme



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# **REPORT OF THE EXTERNAL AUDITOR ON THE REVIEW OF CORPORATE GOVERNANCE AT THE WORLD FOOD PROGRAMME**

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## EXECUTIVE SUMMARY

1. Sound corporate governance, and the effective systems of internal control that go with it, are essential to effective financial management, accountability and transparency. Good corporate governance is necessary to support the achievement of the organisation's objectives and in the creation and maintenance of donor confidence, on which that achievement depends.
2. There has been a considerable evolution in corporate governance in recent years, in both the private and public sectors. The WFP secretariat has also placed emphasis on good governance and is seeking to improve WFP's arrangements in this important area. In the light of these developments, and in this first financial period of my appointment, my staff carried out an initial review of the Programme's corporate governance arrangements to inform future developments at the WFP.
3. There is impetus for change and improvement in WFP, as reflected in the deliberations of the Executive Board and the measures introduced by the Executive Director. My recommendations are intended to assist in this debate. This is an ongoing process but most immediately WFP can strengthen its governance arrangements by:
  - establishing stronger audit committee processes, with the inclusion of non-executive, independent members and better defined reporting to the Executive Director and ultimately, as the arrangements are developed, to the Executive Board;
  - clarifying and formalising the governance roles and responsibilities in the decentralised field structure; and
  - making better use of internal oversight mechanisms, by improving line management accountability for effective responses to audit recommendations.

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## INTRODUCTION

4. High standards and good practice in corporate governance are relevant to all organisations, whether in the private or public sector. Successful organisations have clear objectives; a focus on risk management; operate effective internal control systems; and report their performance reliably and credibly. Confidence in good governance is necessary for achievement and success.
5. Good corporate governance encompasses the fundamental principles of sound accounting and financial management, proper stewardship, accountability and integrity through strong internal controls and transparency of reporting. For the WFP, strong corporate governance provides donors, implementing partners and the beneficiaries of aid with a degree of confidence in the way in which the World Food Programme uses its financial resources.
6. Major corporate failures in several parts of the world and subsequent work to articulate best practice in the private sector, and the high standards required in the public sector, have provided new focus on improvement in governance arrangements to make them more effective and more transparent than ever before.
7. The WFP has been alert to these developments. A Governance Group was established by the Executive Board comprising of members of the Board and other Rome based International Organisations to focus on the administrative and constitutional arrangements for the Board. The scope of the Group covers the role of the Board and its relationship with



the Executive Director and senior management, but does not extend to areas within the competence of the Executive Director.

8. In October 2003, proposals put to the Executive Board by the Executive Director (reference EB3/2003/5-D/1), setting out best practice in oversight mechanisms were welcomed by the Executive Board, which:
  - recognised that WFP had an opportunity to become a leader in corporate governance in the United Nations;
  - appreciated the commitment of the Executive Director to introduce a Statement of Internal Control; and
  - welcomed the Executive Director's proposal to discuss with the Governance Group the possibility of creating an improved Audit Committee arrangement.
9. The proposals raised four areas for immediate consideration: codes of conduct, reporting arrangements, internal oversight committees and risk management. The Office of Oversight is currently working with the Governance Group on these four areas to formulate a business strategy. I commend the initiative being undertaken by the Secretariat in this area.
10. In particular, a Statement on Internal Control (SIC) published with the organisation's financial statements would focus senior executive's responsibilities for ensuring that effective systems of internal control were in place within the organisation and were in operation for the reporting period. To date no UN/International Organisation has produced such a statement in its annual report or financial statements.
11. WFP's Oversight Services Division, OEDO, have recently taken some steps towards the review of best practice in oversight mechanisms, including an initial consideration of governance and risk management issues. Against the background of these developments, my staff looked at the current governance arrangements within the Secretariat focussing particularly on those areas within the scope of the Audit Committee, to inform the current debate and support WFP's development in this important area.

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## AUDIT COMMITTEE

12. The Executive Director carries ultimate accountability for the management of risk and the system of internal control within the organisation. An effective and challenging audit committee is a key element in securing good corporate governance and can be a prime source of assurance for the Executive Director in discharging this responsibility. Internationally there is an emerging consensus on the role of audit committees. In the United Kingdom the Financial Reporting Council<sup>1</sup> defines the purpose of such a committee as being to:
  - monitor the integrity of the financial statements of the organisation;
  - review the organisation's internal financial control system and, risk management systems;
  - monitor and review the effectiveness of the organisation's internal audit function; and

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<sup>1</sup> Audit Committees - Combined Code Guidance, January 2003.



- monitor and review the role and engagement of the External Auditor with the organisation. However, at the WFP this role is undertaken directly by the Executive Bureau and Executive Board.
13. The audit committee should include members who should be non-executives, who should be independent of senior managers.
  14. The Audit Committee at WFP has been an entirely internal body, composed of a chairperson (currently the Deputy Executive Director, Operations) and three members (though currently the members have been confirmed by the Secretariat as: the Deputy Executive Director, Operations; the Deputy Executive Director, Policy and External Affairs; the Associate Director, Operations; the Director, Food Security, Safety Nets and Relief Service; the Chief of Staff and Director, Office of the Executive Director; and the Director, Office of the Deputy Executive Director, Policy and External Affairs). These members are all WFP staff members and all are subject to internal audit oversight.
  15. WFP's Audit Committee has as its terms of reference an objective to ensure the independent role of the internal audit function; and to review their work and consider action in the light of their recommendations. This role includes review and approval of the annual work plan of internal audit and would cover issues pertaining to corporate governance or risk management should they be included in the work plan. WFP has two further internal reporting arms. The investigations unit of the Office of Oversight currently reports directly to the Executive Director; and the evaluations office reports to the Director responsible for results based management.
  16. The present terms of reference of the Audit Committee do not include any formal reporting of their findings or deliberations to the Executive Director or to the Executive Board. Reporting is undertaken on an informal basis from the chairperson of the Audit Committee to the Executive Director. Though this is useful, it does not allow for the fullest discussion and analysis of problems identified by the Audit Committee; nor does it provide an effective and transparent assurance mechanism for the Executive Board as the Programme's top management forum.
  17. Good governance practice advocates the inclusion of independent, non-executive members on the audit committee, with the position of chairperson being taken by an independent member. While the inclusion of executive management on the audit committee can provide valuable information, their presence at every meeting can sometimes inhibit discussion on sensitive areas. The current wholly internal membership of WFP's Audit Committee could also – at least in theory and perception - present issues of conflict of interest, when the subject matter of the committee touches on areas that are or have been the direct responsibility of a member. An independent, non-executive appointee can bring independence and objectivity as well as valuable knowledge and experience to the work of the committee.

**Recommendation 1. I recommend that WFP revise the practice and terms of reference of the Audit Committee to include appropriate arrangements for reporting formally to the Executive Director. In conjunction with the Governance Group, an informal working group of the Bureau, it might also consider its reporting relationship to the Executive Board.**

**Recommendation 2. To afford a greater level of independence and objectivity in the advice available to corporate management, I recommend that WFP should introduce non-executive independent members to the Audit Committee, but I recognise that this is another matter where the practical implementation would need to be considered fully by the Executive Board.**



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## MONITORING OF FINANCIAL STATEMENTS

18. The audit committee should review the significant financial reporting issues and judgements made in connection with the preparation of the organisation's financial statements, and also review the clarity and completeness of disclosure in the financial statements.
19. Where, following its review, the audit committee is not satisfied with any aspect of the proposed financial reporting by the organisation, it shall report its views to the board. The audit committee should monitor the integrity of the organisation's financial controls. The audit committee, in the absence of other arrangements, e.g. a risk committee, should assess the scope and effectiveness of the systems established by management to identify, assess, manage and monitor financial and non financial risks.
20. The Executive Director committed the WFP to submitting its financial statements to the Executive Board in May 2004. During the closure of the 2002-03 biennial accounts, the Audit Committee was involved in the review of the financial statements produced by the Financial Services Department. The Audit Committee's review was based upon the work conducted by Internal Audit on the financial statements in January 2004, prior to them being transmitted to my staff based in Rome. The Audit Committee tasked the Director of Finance Services to address and clarify specific issues raised by Internal Audit.
21. At the end of March 2004, the Audit Committee met once again to review progress in the finalisation of the financial statements. This meeting was attended by Internal Audit, Finance Services and my staff, as observers. At the end of their deliberations which included issues raised by the External Auditor, the Chair of the Audit Committee concluded that the Executive Director could be advised to sign the financial statements and submit them for final external audit. This was an effective and valuable process.

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## REVIEW OF THE INTERNAL CONTROL SYSTEMS

22. The Executive Board approved the decentralisation of WFP to establish Regional Bureaux in the field, to improve communication with host governments and to ensure closer links with the country offices. The decentralisation of the operational aspects of WFP's business has progressed. The administrative aspects have not yet been fully decentralised, with the human resources, budget, fundraising and oversight and evaluation functions still being very centralised.
23. My staff reviewed the internal control and governance structures at headquarters and at each of the Bureaux and country offices visited during the biennium. In doing so it drew upon the work of Internal Audit and the Audit Committee. As a basis for our opinion on the financial statements we were satisfied that the current internal control arrangements were adequate. However there were a number of broader issues relating particularly to the Regional Bureaux and country offices arising for our work.
24. In practice, Country Directors are responsible and accountable for all transactions and operations within the national borders of their assigned country. The Programme's six Regional Bureaux were established to oversee field operations and provide support, guidance and advice to the country offices, while routing project proposals and reporting the collective results and operational performance to headquarters in Rome. Headquarters is responsible for strategic direction and global support and guidance, especially for functions that have not been decentralised, such as oversight and evaluation.



25. Each WFP office at regional and country level reflects the operational structure of Rome headquarters in maintaining programme, finance, procurement functions and so on. Finance officers at country level, for example, have responsibilities to maintain proper and reliable accounting records for the organisation. They have a reporting link to their own country director, but are also responsible to the regional finance office and finance division at headquarters. This applies similarly for other specialists such as procurement. This type of matrix reporting and arrangement of management responsibilities make it important to have clear delegations and responsibilities for individuals, to avoid conflict between programme responsibilities and operational demands on the one hand, and other requirements and regulations on the other.
26. My staff noted that oversight of the implementation of high level strategy, and compliance with directives and regulations, was spread among many individuals within the organisational structure, leading to a lack of clarity over where ultimate responsibility lies and who has ownership of tasks and compliance. During audit visits to each of the Regional Bureaux, my staff found a distinct lack of clarity over roles and responsibilities between different levels of the organisation. The perceived role of the Bureaux was to provide support and guidance to country offices. My staff found that in practice the support and guidance provided was, on the whole, in response to requests from country offices. They noted that some country offices were not seeking support from the Regional Bureaux, under the false assumption that they did not require support or guidance in the implementation of their work.
27. My staff also noted that the operating culture at the country offices seemed to indicate that each office regarded itself as a stand alone business entity, rather than as an integral part of the WFP. They found that many country offices were unaware of the implication of their actions on the financial position of the organisation: while they were acting in the best interests of the country programmes, this sometimes acted contrary to the rules and regulations set up to protect the organisation.
28. My staff found that this problem was to some extent exacerbated by the lack of clarity in guidelines and procedure manuals. As WFP has undergone considerable change in structure and in management control systems with the introduction of WINGS, little work has been carried out on the updating of relevant guidance in a cohesive and holistic manner throughout the organisation.

**Recommendation 3. I repeat the recommendation made by my predecessor that WFP define the respective roles and responsibilities of the Regional Bureaux and country offices and delineate clearly the accountability and monitoring arrangements necessary to ensure the delivery of the Programme's objectives.**

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## RISK MANAGEMENT

29. One of the most important internal objectives of the WFP must be to retain the credibility of its reputation and ensure that a high degree of donor confidence remains with the Programme. Potential risks which are left unmanaged could damage the operational effectiveness of the organisation, and have consequential effects on the level of future funding that donors are willing to provide to the Programme's operations.
30. WFP do not currently undertake a systematic organisational risk assessment and do not maintain a risk register; although they have comprehensive contingency plans for operations, and their emergency needs assessment work attempts to identify where future operational requirements may arise. The value of a risk register and systematic risk





management arrangements is to provide the means to identify and tackle the factors that could adversely effect the organisation and the achievement of its objectives. A risk register allows for assessment of the impact of risks and the allocation of ownership to manage those risks as required.

31. Robust risk management procedures, informed and overseen by the audit committee, are an important role for the committee in achieving improved governance arrangements. The audit committee plays a vital role in raising awareness and communicating senior management commitment to improved corporate governance and effective, systematic risk management. Risk management should not be seen as the province of internal audit and oversight but should:
- Be actively and visibly supported by senior management;
  - Be reinforced by an organisational culture which supports well thought-through risk taking and innovation;
  - Be reflected in the communication of risk management policies to all staff;
  - Be embedded in the organisation's management processes;
  - Be linked to the achievement of objectives; and
  - Include the assessment and management of risks associated with working with other organisations.
32. Within their current work plan, Internal Audit are actively promoting the need to revise the terms of reference of the Audit Committee and is sponsoring the initiative to introduce a formal risk assessment methodology across the organisation. The introduction of corporate governance and risk management should not be seen as the sole province of the internal audit service. While Internal Audit has a role to play in providing assurance to the Executive Director on specific aspects of internal control, good practice indicates that the impetus for improvement in governance, internal control and risk management should come from senior management; and should be implemented through the line managers at headquarters and country office level who will ultimately be responsible for addressing the key risks identified. The Audit Committee thus offers a forum for review of the Internal Audit work plan and outputs; the major findings of internal investigations and management's response; management's response to external audit observations and recommendations; internal control systems; and risk management.
33. I welcome the initiatives driven by the Executive Director to place a stronger focus on risk management, and would encourage strongly further developments in this area.

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## OVERSIGHT ARRANGEMENTS

34. Good governance requires adequate provision for oversight outside the executive process, represented by internal and external audit arrangements. The role of the Office of Oversight Services (OEDO) changed during the biennium with the Evaluation Unit, responsible for oversight of operational best practice, being put under the responsibility of the Results Based Management Division. The remaining elements of OEDO – Investigations and Internal Audit – remained within the responsibility of the Inspector General. The complement of staff was two in the Office of the Inspector-General, four in Inspection and Investigations and 12 in Internal Audit. In October 2003 the Executive Board, by approving the 2004 budget, approved an increase in this staff complement.



35. The approach adopted by Internal Audit is to focus on areas that they have assessed as the most vulnerable in terms of current developments in the organisation, or which directly support ongoing strategic initiatives. The table shows the areas in which Internal Audit has focussed its activity over the past three years.

<b>INTERNAL AUDIT REPORT AREAS:</b>		
<b>2002</b>	<b>2003</b>	<b>2004</b>
2000-01 Financial Statements	Programme Review Committee	Procurement follow up
Data migration to WINGS – legacy systems	WINGS	Computer and telecommunications
Data migration to WINGS – HR/payroll	2002-03 financial statements	Internal controls
Hiring of consultants	Post-delivery commodity losses	Ocean transport services
	Procurement of food and non-food items	Personnel management
	Air transport operations	Fund raising
		Travel entitlements
		HQ inventory management
10 Country office visits	14 Country office visits	24 Country office visits
<i>Source: OEDA</i>		

36. My staff reviewed the action taken by WFP in response to agreed audit recommendations, from both internal and external audit. The results of this review indicated a marked time lag from the date of the recommendation to the agreed implementation by management. Statistics available under the current Internal Audit monitoring system indicate that of the recommendations made in the past year, 11 out of 22 (50 per cent) of the Fundamental recommendations; 152 out of 253 (60 per cent) of the Significant recommendations; and 394 out of 476 (83 per cent) of the recommendations that merit attention, remained outstanding. A total of 15 fundamental and 48 significant recommendations remain outstanding from reports issued over the four years to 2002.
37. Similarly, review of the issues and recommendations raised by my predecessors, the Cour des Comptes, from their audits of the 1998-1999 (reference EB.3/2002/5-A/1/4) and 2000-2001 (reference EB3/2002/5-A/1/5) biennia indicated that there were respectively 16 and 15 recommendations remaining outstanding at the time of preparing this report; and that less than 30 per cent of the recommendations had been implemented fully.
38. The reports currently prepared by Internal Audit for the Audit Committee highlight outstanding issues by each individual quarter but do not give an indication as to the age of the outstanding recommendations or the reason behind their delayed implementation. In the absence of formal reporting by the Audit Committee to the Executive Director and the Executive Board, there is no effective way in which failure to respond to audit recommendations can be addressed.



**Recommendation 4. I recommend that WFP consider what steps might be taken to improve accountability and the effectiveness of line management's response to audit recommendations.**

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## **ACKNOWLEDGEMENT**

39. I wish to record my appreciation for the co-operation and assistance provided by the Executive Director and the staff of the Programme during the audit.



**Sir John Bourn**  
**Comptroller and Auditor General, United Kingdom**  
**External Auditor**

