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Report of the External Auditor on food-related losses

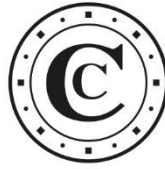
Draft decision*

The Board takes note of “Report of the External Auditor on food-related losses” (WFP/EB.A/2018/6-G/1) and management response in WFP/EB.A/2018/6-G/1/Add.1, and encourages further action on the recommendations, taking into account considerations raised by the Board during its discussion.

* This is a draft decision. For the final decision adopted by the Board, please refer to the Decisions and Recommendations document issued at the end of the session.

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EXTERNAL AUDIT OF THE WORLD FOOD PROGRAMME

AUDIT REPORT FOOD-RELATED LOSSES

Financial year 2017

COUR DES COMPTES REFERENCE: WFP-2017-10

TABLE OF CONTENTS

SUMMARY..... 4

I. AUDIT OBJECTIVES, SCOPE, AND APPROACH 5

II. LIST OF RECOMMENDATIONS 8

III. INTRODUCTION..... 9

IV. OBSERVATIONS AND RECOMMENDATIONS10

1. MAIN CHARACTERISTICS OF LOSSES..... 10

 1.1. Chronology of losses.....10

 1.2. Level of losses11

 1.3. Origin of losses12

2. REPORTING TO THE EXECUTIVE BOARD..... 14

 2.1. Fragmented presentation of losses15

 2.2. Calculation differences between reports.....15

3. FROM THE DEFINITION OF SUPPLY TO THE ORDER 16

 3.1. Selection of vendors.....16

 3.2. Procurement procedure.....16

4. FROM SHIPMENT TO DELIVERY 17

 4.1. Rejections by governments17

 4.2. Inspection companies.....18

 4.3. Insurance19

5. FROM DELIVERY TO THE COUNTRY TO TRANSFER TO THE PARTNERS 22

 5.1. Warehouses22

 5.2. Cooperating partners.....25

6. FROM DISTRIBUTION TO FINAL CONSUMPTION..... 26

 6.1. Distributions by partners.....26

 6.2. Feedback from beneficiaries27

 6.3. Risk of diversion after distribution.....27

7. FOOD SAFETY AND QUALITY 28

 7.1. Quality control system28

 7.2. Quality control limits28

8. INFORMATION SYSTEMS 29

9. VALUATION OF LOSSES 30

V. ACKNOWLEDGEMENTS31

APPENDIX 1 - APPROXIMATION OF COMPLETE COSTS OF LOSSES IN 2016 AND 2017 32

SUMMARY

The World Food Programme distributes 3-4 million mt of foodstuffs a year to the organization's beneficiaries, particularly in zones suffering large-scale humanitarian crises. WFP's food supply chain mobilizes all the links in the organization, from headquarters to country offices, including external service providers called upon by WFP, and cooperating partners distributing foods to beneficiaries.

Despite an environment in which complex emergency situations are multiplying and the risk of incidents is increasing as a consequence, WFP maintains a level of losses of below 1 percent of the foodstuffs it handles. The risk of losses exists at all levels of the supply chain, from foodstuff procurement to distribution, involving an ever-increasing number of actors and procedures.

This variety of actors underlies the heterogeneous perception of the notion of losses in the organization. The level of losses recognized by WFP is limited to those with a direct financial impact for the organization, such that incidents such as delivery delays or returns to suppliers are not included, although they have an impact on the efficiency and effectiveness of operations. In addition to this financial understanding of losses, there are other perceptions of losses on the part of employees in the various units of WFP. The understanding of losses is fragmentary and depends on the use of the data available. This can lead to differences in the accounting of losses between different reports on the issue.

Exhaustive overall monitoring of foodstuff losses has been strengthened in recent years by the introduction of two information systems, LESS and COMET. Each system covers a specific sequence within the supply chain. WFP still lacks an integrated tool with which to monitor losses from procurement through to final consumption. Moreover, WFP's monitoring of overall risks linked to food supply could be improved by real-time recording of foodstuffs.

The organization works with a range of partners to ensure checks on foodstuffs received with the delivery of a load in port as well as the distribution of foods to beneficiaries. The supervisory role of the regional bureaux would benefit from being strengthened, particularly in the monitoring of warehouse inspections and the application of partnerships in the field. The coverage of risks of losses suffered by WFP as a result of partners' actions is conducted through an internal insurance system backed up by external insurance that currently covers only a minority of the losses WFP suffers – pre-delivery losses – and should soon be extended to other losses suffered by WFP.

Ensuring beneficiaries' satisfaction and the response to their needs by improving the monitoring of incidents linked to foodstuff quality and beneficiary feedback is an integral part of an exercise seeking to limit WFP's reputational risk. This calls for strengthening of the internal control mechanisms to prevent illegal use of the food distributed and the rationalization of incident signalling procedures.

I. AUDIT OBJECTIVES, SCOPE, AND APPROACH

1. As announced in our notification letters dated 17 July 2017 and 1 December 2017, a team of five external auditors conducted a verification at WFP headquarters in Rome in two stages, from 11 to 15 September 2017 and from 22 January to 2 February 2018. In addition, all the field missions scheduled in the external offices during the 2017–2018 fiscal year contributed to the preparation of this report.¹ The purpose of this audit was to examine food-related losses.

2. Pursuant to an Executive Board decision of 10 November 2015, WFP External Audit was entrusted to the First President of the *Cour des comptes* of France for the period 1 July 2016 to 30 June 2022, in accordance with Article 14.1 of the WFP Financial Regulations.

3. The External Auditor's mandate is set out in Article XIV of the WFP Financial Regulations and its annex, and in the call for applications for the position of External Auditor. Its terms of reference comprise the call for applications, together with the detailed technical offer of services of the *Cour des comptes* approved by the Board.

4. The responsibilities of the External Auditor consist of auditing the accounts of WFP (Article 14.1 of the Financial Regulations) and making observations, if he sees fit, with respect to the efficiency of the financial procedures, the accounting system, the internal financial controls and, in general, the administration and management of WFP (Article 14.4 of the Financial Regulations).

5. Pursuant to Article 3.1 of the WFP Financial Regulations, the Executive Director is responsible and accountable to the Board for the financial management of WFP activities.

6. A letter of engagement was drawn up with the Executive Director in order to ensure that, in accordance with international audit standards, the respective obligations of management and of the External Auditor are clearly understood. In addition, before each audit, the External Auditor informs the Secretariat of the scope of the audit activities to be undertaken.

7. This report was included in the annual work plan of the External Auditor submitted to the Executive Board at its second regular session in November 2017, which detailed the audits to be carried out between July 2017 and June 2018. Pursuant to the terms of reference, the Auditor shall each year produce an audit report on the financial statements of WFP (submitted to the Board for approval) accompanied by an opinion on the accounts, a report each on the performance and the compliance of WFP management, also known as "performance audits" (submitted to the Board for consideration) and ten management letters issued following field office visits (regional bureaux and country offices). The External Auditor also reviews the draft annual report on the implementation of the recommendations of the External Auditor submitted by the Secretariat to the Board for consideration.

8. The food losses audit was performed in accordance with the International Standards of Supreme Audit Institutions (ISSAI) on performance and compliance audits, WFP's financial regulations, and with the additional mandate appended thereto. These standards obligate the External Auditor to comply with the relevant professional ethics rules with regard to auditing, to exercise professional judgement, and to demonstrate a critical approach throughout the audit.

¹ Regional bureaux in Cairo and Johannesburg and country offices in Kenya, Lebanon, Malawi, Nepal, State of Palestine, Turkey, Ukraine and Zimbabwe.

9. The primary aims of the audit were to:

- identify and quantify, if possible, all the losses of any kind related to food procurement by WFP, from determination of the food basket to final consumption;
- review the identification, analysis, and reporting mechanisms related to food-related losses;
- analyse the effectiveness of the measures put in place to prevent and mitigate these losses.

10. Each observation and each recommendation was discussed with the relevant staff, in particular the staff of the Supply Chain Division (OSC). The partial audit closure meeting was held in the presence of the Director of the OSC Division on 2 February 2018. The Secretariat confirmed the validity of the statements made. This report takes full account of its comments and responses, provided in writing on 26 March 2018.

11. During an audit conducted according to the international standards, performance and compliance are examined on the basis of appropriate criteria, and the causes of any variations from these criteria are analysed. The goal is to answer the main audit questions and to recommend improvements. The first step of the audit is to specify the outlines of the subject matter, i.e., the information or activity to be measured. This subject matter can take various forms and have various characteristics, depending on the audit aim. An appropriate subject matter is identifiable and capable of consistent evaluation or measurement against the adopted criteria, such that it can be subjected to procedures for gathering sufficient and appropriate audit evidence to support the audit opinion or conclusion.²

12. The concept of food-related losses has been addressed in the widest possible sense. All forms of losses have been taken into consideration. Losses that do not result in financial loss, either because they are covered by insurance mechanisms or because they are reimbursed by co-contractors, were within the scope of the audit since they sometimes have an impact on the effectiveness of operations. Similarly, events that result in only indirect financial loss, such as potential disputes with foodstuff vendors, transporters, or central governments, refusals of goods at borders, and incidents related to quality and food safety may cause unforeseen delays and additional costs, undermine WFP's reputation, and ultimately compromise WFP's aims. They were also taken into account.

13. The final aim of this audit was to assess whether WFP's internal control mechanisms, which should enable it to reduce all these losses to an acceptable level, are adequate.

14. In order to examine the quality of internal control of losses, the External Auditor drew up a logical framework of the underlying aims pursued by WFP, classifying them into three categories as immediate, operational or strategic. To achieve each type of aim, a programme targets outcomes of varying types: immediate aims are translated into factual achievements; operational aims assume that results are obtained, which calls for a more qualitative assessment; strategic aims are manifested through expected long-term effects, the analysis of which is more of an evaluation. The expected achievements, results, and effects identified in the logical framework constitute the base criteria for assessing the performance of the operation. The degree of complexity in assessing the achievement of the aims varies according to their status, and in some cases, particularly in terms of ultimate effects, it often exceeds the limits of a performance audit. The approach to a programme based on the logical framework of aims can be summarized as indicated below.

² Standard ISSAI 100, paragraphs 22 and 26.

Immediate aims	Operational aims	Strategic aims
<ul style="list-style-type: none"> • Evaluate suppliers (plant inspection, certification); • Establish procurement requirements (contents and packaging); • Detect sanitation problems/check condition of commodities, including commodities transferred to cooperating partners (CPs); • Train WFP staff to intervene in case of food-related incidents; • Give access to storage and train small farmers; • Adapt internal procedures to Purchase for Progress (P4P); • Adapt to beneficiaries' constraints; • Collect necessary data to monitor food commodities. 	<ul style="list-style-type: none"> • Ensure distributions in the best times; • Obtain products consistent with the criteria; • Guarantee the good condition of the commodities throughout the supply chain; • Monitor the activity of operational partners; • Compliance with standards and regulations of governments involved; • Limit contamination and improper post-collection manipulation of smallholders; • Ensure rigorous internal control on food supplies; • Monitor and consolidate cases of observed losses. 	<ul style="list-style-type: none"> • Sort out financial losses; • Prevent fraud; • Address reputational and legal risks; • Provide a sufficient supply in quantity and quality (nutrients) to target populations; • Take into account all constraints (climate, culture, price, availability, etc) according to the intervention context; • Ensure that small farmers produce in compliance with standards and quality requirements; • Innovate to improve product storage times and characteristics.
Actions	Results	Expected effects

Source: External Auditor

II. LIST OF RECOMMENDATIONS

15. The recommendations are classified by order of priority:

- **priority 1.** a fundamental issue requiring immediate attention by management.
- **priority 2.** less important checkpoint that should be addressed by management.
- **priority 3.** point on which checks could be improved and to which management's attention is drawn.

Context	Priority	Recommendations
Reporting to the Executive Board	2	Recommendation 1. The External Auditor recommends improving reporting to the Executive Board by providing an annual report on losses whether they occur before or after delivery, irrespective of any amounts insured or reimbursed.
Selection of vendors	1	Recommendation 2. The External Auditor recommends continuing to strengthen the order management procedures: a) by implementing a tool to manage international, regional, and local vendors as soon as possible, so as to allow WFP to have a global view of vendors and their services; b) by upgrading the WINGS software or developing an alternative solution to have a global view of the performance of its contracts and be able to perform extractions with a view to effective management.
Inspection companies	1	Recommendation 3. The External Auditor recommends developing a system making performance statistics on surveyors and superintendents available at the organization level.
Self-insurance	2	Recommendation 4. The External Auditor recommends expanding the information submitted annually to the Executive Board by adding the financial statements of the special self-insurance account; and a report on the appropriateness of the level of insurance reserve.
Warehouses	1	Recommendation 5. The External Auditor recommends strengthening the control of warehouses: a) by inviting country offices to plan inspections based on a risk analysis; b) documenting and keeping records of the inspections conducted; c) organizing documented monitoring of the frequency of warehouse inspections carried out by country offices.
Cooperating partners	2	Recommendation 6. The External Auditor recommends: a) centralized collection of the agreements entered into with the partners; b) making the performance of partnership agreements in the field a priority area of oversight implemented by the regional bureaux.
From distribution to final consumption	1	Recommendation 7. The External Auditor recommends: a) extending beneficiary feedback mechanisms to all regional bureaux; b) examining the possibility of strengthening the procedures for detecting illegal uses of distributed food.

Context	Priority	Recommendations
Food safety and quality	2	Recommendation 8. The External Auditor recommends strengthening internal quality control: a) by forwarding all inspection reports to the Food Quality and Safety Unit (OSCQ); b) by establishing an exhaustive information system on quality incidents allowing the OSCQ unit to perform monitoring and management; c) by continuing the deployment of the quality assurance system in order to reduce the organization's dependence on one-off product inspections.
Information systems	2	Recommendation 9. The External Auditor recommends striving for real-time data recording in LESS in order to set up this system as a true food commodities tracking system.

III. INTRODUCTION

16. In 2017, the World Food Programme (WFP) distributed 3.9 million mt of food³ and handled 4.5 million mt, particularly in countries experiencing acute crises.

17. The term "food commodities" refers to all food products purchased or received by WFP and intended for beneficiaries for the provision of direct food aid. This includes raw foods, processed foods and specialized nutritious foods (SNF), whether distributed by WFP itself or through its partners. Food aid provided to beneficiaries through cash-based transfers was excluded from the scope of this audit.

18. A limited portion of this food does not reach the intended recipients in the planned conditions. It represents 28,477 mt, worth USD 20.5 million in 2017, i.e., 0.82 percent of total foodstuffs handled annually by value.⁴ These losses are observed at various stages of the supply chain and can take many forms: theft, fraud, disappearance of quantities, deterioration of quality, unsuitability for local specific needs leading to destruction, etc.

19. Their causes themselves vary: unsuitable product at departure, losses at sea, excessive storage time, looting, and fragile packaging being among the most frequent. A significant portion of the losses can be seen in countries experiencing internal or external conflicts, which is not surprising since these areas call for the largest deliveries and involve the biggest operational challenges.

20. These losses are monitored in two information systems. In this case, the systems are LESS, up to the transfer of custody of the food to a government counterpart or cooperating partner who will ensure its final distribution, and COMET beyond this transfer.

21. This audit report sought to identify all food losses, to analyse their causes, and to propose improvements to better determine and reduce them.

³ Amount distributed to beneficiaries, to WFP cooperating partners and government counterparts with a view to final distribution. Of this amount, USD 3.5 million reached final beneficiaries (provisional data of 25 January 2018).

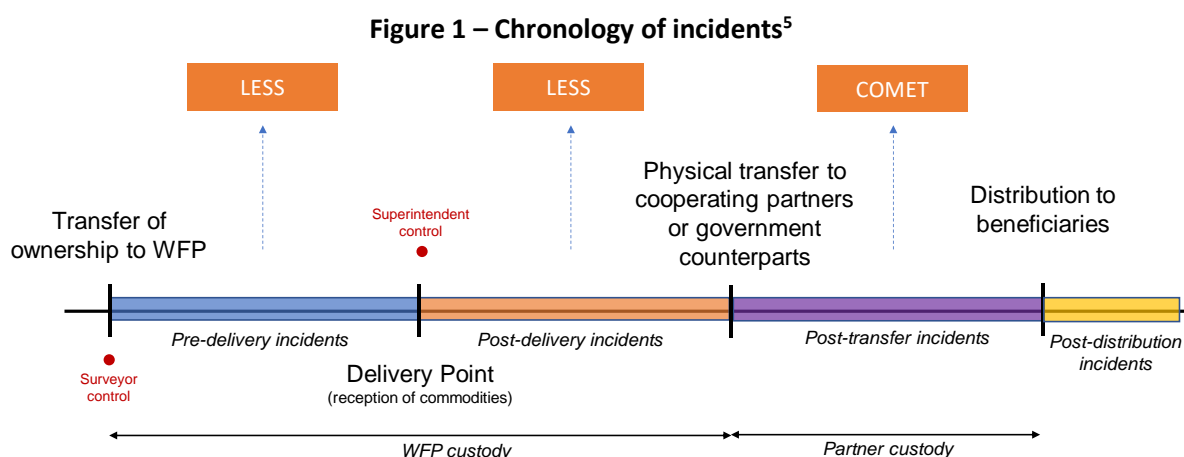
⁴ Provisional data.

IV. OBSERVATIONS AND RECOMMENDATIONS

1. Main characteristics of losses

1.1. Chronology of losses

22. WFP's food losses can occur at various stages of the supply chain, which runs from purchase from the vendor or reception of an in-kind donation to consumption by the beneficiary. Depending on the stages at which they occur, they are recorded by different systems and means.



Note: The check carried out by the superintendents is only performed at ports at which loads transported by sea are offloaded. At the request of the country office, superintendents can also carry out tallies of foods received by the office via land transport. In the case of foods received by WFP as in-kind donations, checks are performed by the donors themselves and certified by documents WFP receives from them.

Source: External Auditor

- **Pre-delivery losses.** Losses that occur between the vendor's shipment and the first delivery point in the recipient country are recorded and tracked in terms of volume and value using the LESS information system. Identified in WFP's terminology as pre-delivery losses, they affect goods that are the property of the organization. If the recipient country is not the country of entry of the goods, the pre-delivery phase extends to the point of entry into the recipient country.
- **Post-delivery losses.** Losses that occur between the first point of delivery in the recipient country and the delivery of foods, i.e., either directly to the beneficiaries or, in the majority of cases, to cooperating partners for their final distribution, are also tracked in the LESS module. They are identified in the WFP terminology as post-delivery losses. Ownership of food products is usually transferred to the government of the beneficiary country where these commodities are to be distributed. Even though ownership of food products stored in its warehouses has been transferred, WFP recognizes them as inventory because it retains physical custody and control of them.⁶ WFP itself generally routes them to the point of distribution to partners or beneficiaries.

⁵ Some losses are reimbursed or replaced by vendors so do not turn into a direct financial loss. These are generally referred to as incidents.

⁶ Note 2.4 to the financial statements.

- **Post-transfer losses.** Losses that occur after the transfer point are beyond WFP's control, which means that it no longer has custody of the food products. The food commodities cease to be assets of the organization, but it retains a duty of care with regard to their use. It is important to distinguish within this phase an initial sequence from the delivery of food commodities to cooperating partners or governments, which ensure their storage, up to their final distribution. This phase is called "post-transfer incidents" in figure 1 above: WFP no longer has custody of the food commodities, having distributed them to government counterparts or cooperating partners, but they have not yet been distributed to the beneficiaries. The volumes of losses that may occur during this sequence are tracked in the COMET electronic module on the basis of information available in the distribution reports.
- **Post-distribution losses.** Losses that may occur after distribution to the beneficiaries, for example because of diversion or impediments to consumption, are not tracked in a particular information system.

1.2. Level of losses

23. In 2017, according to the available information,⁷ the volume of food losses (before reimbursement by insurance and recoveries from vendors and transporters) increased⁸ to 28,477 mt, valued at USD 20.5 million, which represents 0.73 percent of the distributed food in volume and 0.93 percent in value. As regards food commodities stored in 2017,⁹ including both foods stored at the start of the year in recipient countries and foods received by countries during the period, losses represented 0.63 percent of the total volume and 0.82 percent of the value. These loss figures show satisfactory logistical performance, since over the past five years, losses have remained below 1 percent of transactions with a fairly stable level in recent years. In 2016, losses represented 0.74 percent of the stored food commodities in volume and 0.96 percent by value.

Table 1: Change in pre- and post-delivery losses between 2013 and 2017

Year	Pre-delivery losses		Post-delivery losses		Total net losses by volume (mt)	Total net losses by value (USD)
	Net losses by volume (mt)	Net losses by value (USD)	Net losses by volume (mt)	Net losses by value (USD)		
2013	11 268	7 498 680	25 016	18 684 094	36 284	26 182 774
2014	9 324	8 135 847	18 921	15 563 533	28 245	23 699 380
2015	14 483	8 064 549	12 694	11 019 934	27 177	19 084 483
2016	10 791	6 084 737	20 109	18 070 937	30 900	24 155 674
2017	11 199	5 939 588	17 278	14 598 416	28 477	20 538 004
Total	57 065	35 723 401	94 018	77 936 914	151 083	113 660 315

Note: 2017 post-delivery losses (USD 14.6 million) include losses after hand over to cooperating partners and government counterparts, which amount to USD 2.5 million.

Source: External Auditor, on the basis of data provided by WFP. 2017: Provisional data as of 24 January 2018, LESS extraction and Supply Chain Division (in charge of drafting the report on post-delivery losses dated 21 March 2018).

⁷ Provisional data from the General Accounts Branch (RMFG) and OSC.

⁸ Amount distributed to beneficiaries, to WFP cooperating partners and government counterparts.

⁹ Provisional data from OSC.

24. **However, this satisfactory performance must be put into perspective. In order to be exhaustive, a picture of food-related losses should also take into account incidents or events that do not result in direct financial loss but that nevertheless amount to a loss of efficiency and effectiveness: additional costs generated by an incident, delivery delays, tax exemptions not respected, insurance costs, lawsuit and court costs, etc. are all additional costs that qualify the performance of a supply operation.**

25. The valuation of losses used by WFP to track data in LESS and COMET includes, in addition to the cost of food products at their purchase price, any other associated cost during the transport of food and any additional food processing costs.¹⁰

26. By contrast, the figure cited above does not take into account certain events or costs associated with incidents:

- additional costs related to additional storage times, re-export to another country, or additional loss management measures (destruction costs, laboratory tests, cleaning, inspections, etc.);
- insurance costs as well as costs of managing claims against third parties;
- food commodities returned to the vendor are not considered a loss, since there is no financial loss, but the operation at least results in increased delivery times and loss of effectiveness;
- undelivered food commodities deducted from the vendor's or transporter's invoice are also not taken into account, even if WFP has implemented mechanisms to replace the missing food commodities, even a temporary difference between the intended quantity and the quantity delivered can also be analysed as a loss of effectiveness.

27. On the other hand, it should be noted that the losses indicated in value in LESS are gross losses, before payment of compensation by insurers and before recoveries with vendors and transporters.¹¹

28. Lastly, disputes in which WFP is a party also represent a potential additional cost associated with the organization's aid operations and food assistance, part of which is directly related to food procurement and distribution. This cost can be estimated at around USD 30 million as of 31 December 2017. It mainly comprises VAT credits non-reimbursable to WFP by certain states (USD 29 million¹²), the rest derives from debts associated with disputes between WFP and third parties. These receivables were written down and provisions established for payables.

1.3. Origin of losses

¹⁰ The WFP Policy Guidance Manual for International Public Sector Accounting Standards defines the cost of food losses using the following formula: *"The cost of food commodities includes purchase cost or fair value if donated in-kind and all other costs incurred in bringing the food commodities into WFP's custody at their point of first entry into a recipient country where they become distributable. In addition, any significant costs of conversion such as milling or bagging are included. Cost is determined on the weighted average basis"*.

¹¹ Appendix 1: Approximation of complete costs of losses in 2016 and 2017.

¹² This figure includes all types of payments (service providers, material, fluids, etc.), not just food procurement.

29. In 2017, nearly 81 percent of the volume¹³ of pre- and post-delivery losses was due to problems with transport and storage of food commodities.¹⁴

Table 2: Top five causes of total losses in volume in 2017

Transport	<ul style="list-style-type: none"> • 10,768 mt • USD 5,829,755 • 0.31% of food distributed to beneficiaries • 0.24% of food commodities handled • 45.9% of total losses in volume
Excessive storage time	<ul style="list-style-type: none"> • 5,015 mt • USD 3,979,128 • 0.15% of food distributed to beneficiaries • 0.11% of food commodities handled • 21.4% of total losses in volume
Damage due to storage	<ul style="list-style-type: none"> • 3,196 mt • USD 2,918,443 • 0.09% of food distributed to beneficiaries • 0.07% of food commodities handled • 13.6% of total losses in volume
Vendor issues	<ul style="list-style-type: none"> • 2,318 mt • USD 3,309,230 • 0.07% of food distributed to beneficiaries • 0.05% of food commodities handled • 9.9% of total losses in volume
Product breakage during handling	<ul style="list-style-type: none"> • 1,136 mt • USD 793,342 • 0.03% of food distributed to beneficiaries • 0.03% of food commodities handled • 4.8% of total losses in volume

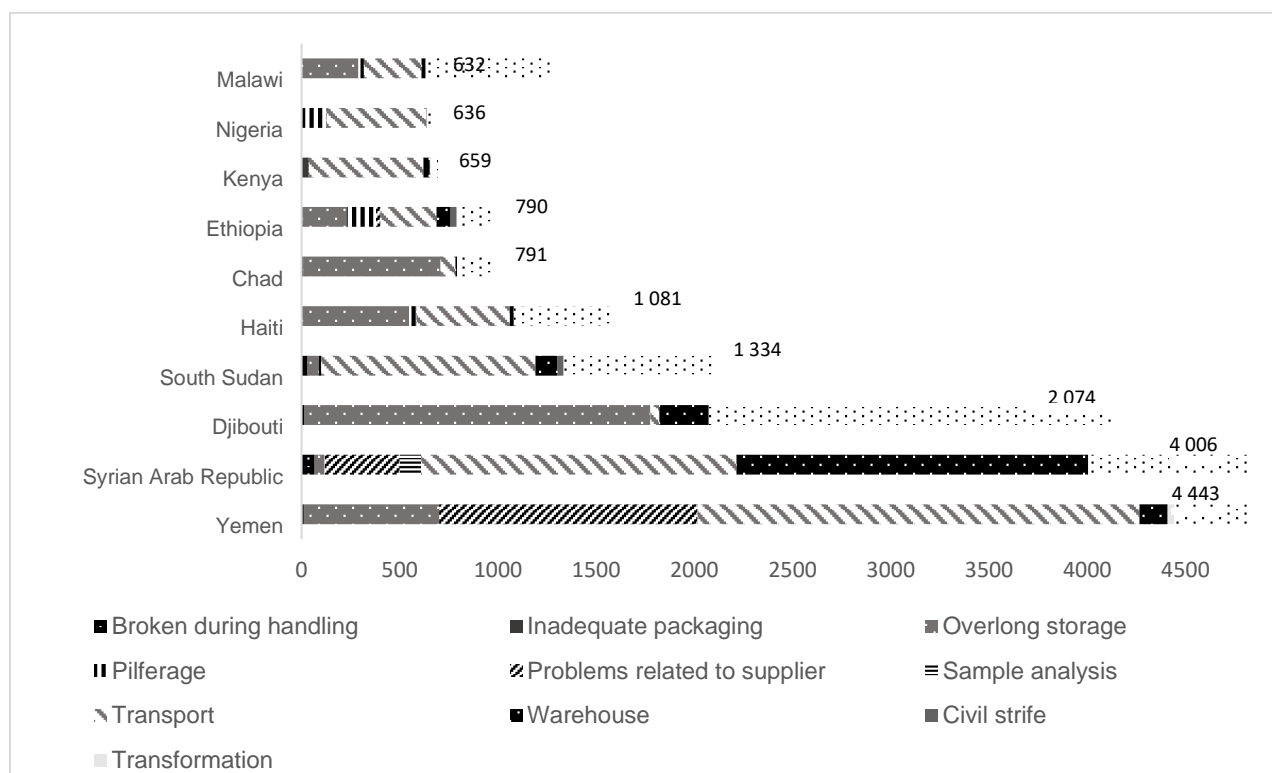
Source: External Auditor, on the basis of pre-delivery losses and post-delivery losses identified in LESS for 2017. These data do not include post-transfer losses, when commodities are under the responsibility of cooperating partners.

30. Excessive storage time and inadequate transport are long-standing loss factors, but in recent years, losses caused by looting in conflict areas have been significant, particularly in the Syrian Arab Republic, South Sudan, and Yemen.

¹³ The calculations and figures presented here are based on provisional data from January 2018.

¹⁴ The calculation includes transport (45.9%), excessive storage time (21.4%) and warehousing (13.6%).

Figure 2: Ten countries with highest total losses in 2017 (mt) and causes of these losses



Source: External Auditor, based on LESS data as at January 2018.

31. For 2017, pre-delivery losses accounted for 28.9 percent of losses by value and 39.3 percent of total losses by volume, while post-delivery losses before transfer to partners represented 47.8 percent of losses by volume and 59 percent of losses by value. Adding to these figures the share of losses after transfer of food commodities to WFP's partners, **the share of losses after delivery up to the final unloading point represents 71.1 percent of total losses by value and 60.7 percent of losses by volume.**

32. Since 2013, losses by volume have decreased by 21.5 percent and losses by value by 21.6 percent.

2. Reporting to the Executive Board

33. The Executive Board is informed of losses of food commodities during the annual session in June through two documents:

- The annual Financial Statements submitted to the Executive Board in accordance with Article XIV-6 (b) of the WFP General Regulations and Articles 13.1 and 14.8 of its Financial Regulations. These financial statements are prepared by the Resource Management Department (RM), certified by the Executive Director, and presented to the External Auditor no later than 31 March following the end of each fiscal year. In accordance with Article 12.4 of the Financial Regulations, the financial statements are accompanied by a statement that indicates the value and volume of food product losses.

- The annual report on post-delivery losses, prepared by the Operations Services Department (OS), which details food losses that occurred during the previous fiscal year and the measures taken to minimize the risks of new losses. As the name indicates, this report does not address losses before delivery.

2.1. Fragmented presentation of losses

34. Reports to the Executive Board are not exhaustive. They are limited to post-delivery losses in recipient countries, not to mention the methodological limitations mentioned in the previous chapter. Note 9 to the 2016 financial statements (WFP/EB.A/2017/6-A/1) indicates that “food commodity losses occurred after the related food arrived at the recipient country”. The 2016 annual report on post-delivery losses (WFP/EB.A/2017/10-B) states that it “does not cover pre-delivery losses or unintended uses of food after distribution to beneficiaries”.

35. The Secretariat considers that it should report post-delivery losses specifically as they concern food commodities of which ownership has been transferred to recipient States.

36. The External Auditor considers that the Secretariat should account for all losses regardless of when they occur in order to inform members about the overall handling of food commodities.

2.2. Calculation differences between reports

37. The 2016 financial statements, certified at the end of March 2017 and presented to the Executive Board at its annual session, in June 2017, showed post-delivery food losses of USD 21.1 million. In the report on food commodity losses, also presented to the Executive Board at its annual session in June 2017, post-delivery food losses were USD 18.1 million.

38. According to the Secretariat, this discrepancy of USD 3 million is due to a difference in the sources of information taken into account by the two reports. The financial statements are based on the posting date of the loss, which should be posted as far as possible in the accounting period during which the event was noted; the report on losses is based on the date of the document certifying the existence of a loss. The document date may be outside the accounting period.

39. These discrepancies are more or less significant depending on the year and are reconciled by the Finance and Treasury Division (RMF), which ensures that they do not come from different event recognition dates rather than errors. Although at first glance these are not errors in the calculation of amounts, these differences resulting from discrepancies undermine the Executive Board’s information.

40. The Finance and Treasury Division indicated that for 2017, the Secretariat will strive to apply the same posting date for both reports.

Recommendation 1. The External Auditor recommends improving reporting to the Executive Board by providing an annual report on losses whether they occur before or after delivery, irrespective of any amounts insured or reimbursed.

3. From the definition of supply to the order

3.1. Selection of vendors

41. For international purchases, WFP relies on a pool of previously selected vendors. This pool does not include all local and regional vendors, which are managed in local and regional pools without the involvement of headquarters in Rome.¹⁵ Therefore, at the headquarters level, WFP does not have a global, comprehensive vision of the commodities vendors that it uses.

42. In 2014, the External Auditor recommended the implementation of a vendor management system, which would have made it possible to update the database, ensure that vendors meet their regulatory requirements, and monitor the status of vendors (under sanctions, suspended, or still under contract with WFP).

43. To date, this management tool, which would provide an overview of all the vendors with which WFP works, is not yet available. WFP indicated that the budget provided for the implementation of this software in 2018, with the help of an external service provider.

44. Any company wishing to be part of the pool of WFP international food commodity vendors must undergo a selection procedure, which the External Auditor considers to be rigorous. The company must first complete the initial paper assessment, a questionnaire to determine whether it meets WFP's requirements in terms of quality and safety, production capacity, and technical equipment. This document is very precise and provides extensive information about the candidate company. At the same time, several documents¹⁶ are required from these companies.

45. Field surveys tend to show that the selection process for local and regional vendors may be less demanding, which is also due to the size of the companies involved. The updating of the vendor list, which must be annual,¹⁷ was not respected in four of the ten offices visited.¹⁸ This type of situation could convey complacency with regard to vendors already present in the pool.

3.2. Procurement procedure

46. The External Auditor considers that the proportion of contracts affected by a delay and the number of contract defaults across all contracts entered into by WFP are basic data, which would seem to be necessary for managing the procurement function. WFP does not challenge

¹⁵ The headquarters' pool could, however, include local and regional vendors, if the latter meet the criteria required for inclusion in WFP's international vendor pool.

¹⁶ Three commercial references; proof of registration on the United Nations procurement portal, United Nations Global Marketplace (UNGM); the company's articles of association (to guarantee the lawful existence of the company, its existence for at least three years, and its entry in the legal registers); the company's financial statements for three years proving a turnover of EUR 5 million to verify the company's ability to honour its contract; and an export licence.

¹⁷ Section 11 of the Food Procurement Manual.

¹⁸ Cairo and Johannesburg regional bureaux and Nepal and State of Palestine country offices.

this analysis, but despite several requests, the latter was unable to provide these data: the information system, WINGS (in SAP format), does not allow for the extraction of data for comparisons and global analyses of contracts. The absence of this functionality is detrimental in terms of management and reporting for WFP. To date, only contract-by-contract tracking is possible.

Recommendation 2. The External Auditor recommends continuing to strengthen the order management procedures: a) by implementing a tool to manage international, regional, and local vendors as soon as possible, so as to allow WFP to have a global view of vendors and their services; b) by upgrading the WINGS software or developing an alternative solution to have a global view of the performance of its contracts and be able to extract data with a view to effective management.¹⁹

4. From shipment to delivery

47. WFP mainly uses maritime transport for the delivery of supplies. The selection of maritime transport providers follows the professional practices of this field. Shipping companies are not selected directly. WFP uses intermediaries who propose service providers to them depending on the type of cargo.

4.1. Rejections by governments

48. Rejections of WFP deliveries by governments of recipient countries are handled by the country offices. The offices inform headquarters only of major incidents on a case-by-case basis. The ten major incidents in 2016-2017 involved the Syrian Arab Republic, Yemen, Egypt, Burkina Faso, as well as the ports of Latakia and Tartus (Syrian Arab Republic), and Beirut (Lebanon).

49. These rejections of food commodities can result in additional costs related to their destruction, rerouting to other countries if they are in good condition, repackaging, reselling (animal feed), or return to vendors.

50. In 2016, these returns to vendors,²⁰ net of products supplied by the latter as replacement, represented 7,179 mt and USD 4,131,994 in food commodities for quality reasons, incomplete arrival, or damaged shipments. Relative to total losses for the year after the addition of returns to vendors, these returns to vendors represent 18.9 percent of WFP's operating losses by volume and 14.6 percent by value. In 2017, total returns to vendors represented 584 mt of food commodities with a total value of USD 267,913.²¹

51. A number of examples serve to illustrate the reasons for these rejections:²² WFP received in 2016 in-kind donations of food commodities intended for Yemen which had already passed their use-by date, resulting in a loss of USD 229,954 for 182.6 mt of vegetable oil, after destruction. That same year, 917.5 mt of wheat flour purchased by WFP for Iraq, of which the use-by date was too close to the delivery date in the recipient country, resulted in a cost of

¹⁹ The External Auditor will take into account the results of the external review of the vendor management system in progress at the time of the audit in order to review the implementation of this recommendation.

²⁰ Based on a LESS extraction – MB51 based on the reference dates of the documents certifying returns to vendors in 2016 (comparison of movements 122,123, 101, 102).

²¹ Same as above, for 2017.

²² Reports from May 2017 submitted to "Board of Directors for the Oversight and Governance of the Insurance Function"

USD 762,116.5 for the organization, of which USD 395,224.95 was an extra cost to pay for unloading of the food commodities at the port of arrival.

4.2. Inspection companies

52. Quantity and quality are verified by a third-party quality and control (“Q&Q”) surveyor²³ when WFP takes possession of the food commodities. The quantity of goods and their apparent condition when received at the port of unloading is verified by a third-party superintendent.²⁴

53. Superintendents and surveyors are selected through a competitive process. These calls for tenders are one-off when a single cargo is to be verified. When purchases are frequent in a country, as is the case in Turkey, the organization attempts to use a call for tenders to enter into a long-term agreement with an inspection company. It deems that service is frequently better under long-term agreements.

54. For the performance of the Q&Q surveyor’s duties, service providers are selected on the basis of a shortlist of inspection companies located around the world (Baltic Control, Bureau Veritas, Intertek, Saybolt, SGS. Schutter, Control Union Rotterdam, Commodity Inspection Services, Overseas Merchandise Inspection).

55. These same companies can perform the superintendent’s inspection duties during the unloading of ships when they are located at the port of arrival. SGS is established in more than 53 recipient countries, Baltic Control in 31 countries, Bureau veritas in 30 countries, and Saybolt in 23.

56. However, in certain ports, monitoring of unloading can be entrusted only to a small number of locally established companies or a government monopoly (Angola – Intertek, Lebanon – SGS Lebanon, Cameroon – SGS, Congo – Intertek, National Office – Overseas Merchandise Inspection, Egypt – SGS Egypt, Ghana – Intertek, Ukraine – Baltic Control or Bureau Veritas).

57. WFP’s regulations permit the use of the same company for the departure and arrival of a shipment in the roles of surveyor and superintendent.²⁵ If WFP believes that there is no risk of conflict of interest for two inspectors that are part of the same group,²⁶ even if it is through a franchise, and the External Auditor acknowledges that in any case, this situation is sometimes unavoidable.

²³ Food Procurement Manual 4-1-9: “To ensure that both the Q&Q of the goods are in accordance with the terms of the contract, the CO/RB arranges a Q&Q survey to take place immediately prior to WFP taking over ownership of the goods, as specified in the contract. The purpose of this survey is to ensure that both the quantity and quality of the goods are in accordance with the terms of the contract and that all other terms and specifications, such as timing and packaging, are complied with”.

²⁴ Transport manual 5.3.1: “superintendents are independent cargo surveyors, employed by the Programme to inspect WFP consignments, and ascertain their quantity and condition on delivery. Superintendents attend at delivery and issue a report”.

²⁵ Food procurement manual, Article 15-2: “sometimes the same agreement includes both superintendence and surveying”

²⁶ In 2014, the internal audit report on procurement indicated in some cases a risk of conflict of interest in that the inspector responsible for the quantitative and qualitative survey was the same one selected to verify whether the vendors met the conditions required to supply goods to WFP. The procurement unit feels that this situation is not representative.

58. Monitoring the performance of this type of service provider is envisaged in the WFP manuals. Individual surveyor and superintendent performance checklists exist but there is actually no centralized monitoring of the performance of these inspection companies at the level of WFP. However, inspection service providers are few in number and even have a monopoly position in some countries. Better knowledge of their services over time would enhance the ability of the factors used to select from among several candidates and would undoubtedly improve the organization's bargaining power in case of a single service provider. The issue of the organization of monitoring, by establishing performance statistics or other means, for example, is worth addressing.

Recommendation 3. The External Auditor recommends developing a system making performance statistics on surveyors and superintendents available at the organization level.

4.3. Insurance

4.3.1. Self-Insurance Retention Scheme

59. The Self-Insurance Retention Scheme (also known as "The Captive") established in 1993 allows WFP to insure food products during the phase before delivery to the destination country. According to WFP, this self-insurance allows intervention in zones not covered by private insurance and enables it to negotiate premiums well below market prices.

60. Self-insurance covers eligible losses on the insurance market representing up to USD 750,000 in losses per load or USD 1.5 million for two or more consignments on one vessel.²⁷ Above these amounts, the external insurance policies placed with reinsurers apply.

61. The Captive collects premiums, pays compensation, initiates actions of recoveries with third parties, reinsures catastrophic losses and maintains an insurance-loss reserve²⁸ large enough to cover future compensation payments.

62. Although it offers extensive cover, self-insurance operates under the terms of external commercial insurance policies and according to the standards and procedures of the insurance market. As a result, not all losses are covered by this insurance, including in case of pre-delivery losses. Insurance usually excludes losses under the insured's control or that are unavoidable.²⁹

63. WFP's goods are currently insured up to the delivery point in the recipient country, and all losses occurring after they are dropped off are considered post-delivery losses. This arrangement is consistent with the principle that cargo legally belongs to the recipient government once it arrives at its destination.

²⁷ The Captive insures the commodities on "all-risks" terms covering all losses up to USD 750,000 per shipment or USD 1,500,000 for two or more consignments on one vessel. (p.16 Insurance Report, May 2017).

²⁸ An insurance reserve is an estimate of an insurer's liability for future claims.

²⁹ Loss associated with defects in loading cargo are inevitable (cargo loaded already unsafe for consumption) as are losses associated with deliberate misconduct by the insured, cases of insufficient or improper packaging, and losses directly attributable to war situations.

64. A significant portion of WFP's losses are post-delivery losses, which represented an average annual loss of USD 15.6 million from 2013 to 2017 – compared with an annual average of USD 7.1 million for pre-delivery losses.

65. However, in most cases, WFP not only unloads the goods at the unloading port but arranges intermediate storage and handles the inland transport of goods to beneficiaries or cooperating partners.

66. In recent years, donors have expressed reluctance to bear these losses and have requested that WFP refinance the cost of food not distributed to beneficiaries, including goods taken by armed groups, as was the case in the Syrian Arab Republic.

67. The last report submitted to the Executive Board proposed an extension and an "expansion" of the cover.

- **extension** of the cover to start when WFP takes possession of goods until they are physically handed over to cooperating partners, governments, or beneficiaries.
- **expansion** of the cover to include all losses, including those typically not covered by conventional commercial insurance.

4.3.2. Situation of the special account

68. As authorized by the Financial Regulations,³⁰ a Self-Insurance Special Account was established to track the self-insurance activity. According to WFP's management plan,³¹ it allows balances to be carried over from one fiscal year to the next.

69. Contrary to the provisions of the Executive Director's circular dated 27 March 1998³² ("the status of the International Cargo Self-Insurance Special Account shall be reported to the Executive Board in the biennial WFP Financial Statements"), the status of WFP's self-insurance special account for international cargo is not the subject of a report in the annual financial statements presented to the Executive Board. Instead, this account is described in section V of the management plan, but it contains no figures.

70. The mechanism for carrying forward surpluses allowed this special account to establish a cumulative surplus of USD 35.7 million in 2017, up 25.7 percent over five years (USD 28.4 million in 2013).

71. The special account circular provides that "at some time in the future, when sufficient surpluses have been generated, the Executive Director shall report this and present proposals for its use and approval by the Executive Board".

72. The External Auditor wondered about the appropriate level of premiums paid by WFP and the interest in generating a cumulative surplus of USD 35 million, given the surplus trend observed in the special account's income statement over the last five years. Up until 2017, the Operational Risk Management Unit (OSCR) targeted an insurance reserve of USD 20 million, representing approximately two years of compensation payments.³³ In addition, the surplus

³⁰ Article 5.1 of the Financial Regulations: "Trust funds and special accounts may be established by the Executive Director for specified purposes consistent with the policies, aims and activities of WFP. The Executive Director shall report all such trust funds or special accounts to the Board".

³¹ Management Plan (2018–2020), section V.

³² Circular ED98/010

³³ Meeting of the Insurance Supervisory Board, Rome, 10 May 2017, p.21.

exceeding the required reserves has been paid back to WFP several times: USD 10 million in 2002, USD 15 million in 2007, and, for the last time, USD 10 million in 2011.

73. In 2016, OSCR proposed to the Board of Directors for the Governance and Oversight of the Insurance Function a USD 10 million withdrawal from the reserve. This withdrawal can be explained by the desire to use these additional funds for the extension and expansion of the self-insurance policy approved by the Executive Board in November 2017. At the time of the audit it had not yet been presented to the Executive Board.

74. The minutes of the May 2016 Governance and Oversight Committee meeting provide some indication of the level of the insurance reserve. The extension of the cover should more than double the covered losses, which would justify, according to the Secretariat, the reserve being doubled to USD 40 million. The amount of the reserve depends on the trends observed in losses in previous years as well as the time lag between the payment of premiums on shipments and future claims on these same shipments ("The purpose of the reserve is to fund future claims on shipments on which premiums have already been paid"). It should be based on medium-term forecasts on the amount of losses as well as the inflows and outflows of resources to justify the amount.

Recommendation 4. The External Auditor recommends expanding the information submitted annually to the Executive Board by adding the financial statements of the special self-insurance account; and a report on the appropriateness of the level of insurance reserve.

4.3.3. Balance sheet of the Captive

75. WFP indicated that it performed a calculation (not audited) of the savings from using the Captive rather than using external insurers: the insurance policy offered by the Captive would offer premiums on average 43 percent less expensive than those available on the market, which would translate into annual total savings of USD 7.16 million. The Captive can also cover losses that, under commercial cover, would not be reimbursed.

76. On the other hand, the Captive is a mechanism whereby WFP pays insurance premiums to itself, pays any compensation to itself, sets up reserves in its own consolidated accounts and pays any reserve surplus back to itself. The External Auditor wonders if the cost of operating the system (USD 1.29 million) could be saved by WFP managing it directly without resort to a special account.

77. There are several arguments for maintaining the mechanism:

- it is difficult for donors to accept that the value that they have funded has been lost; provisions should therefore be established in any case;
- WFP should continue to carry out recovery actions with its partners. Consequently, most of the administrative work and the corresponding costs would be the same;
- our simulations did not show any realizable savings with a switch to direct management.

78. It may be considered that the self-insurance mechanism has the advantage of clearly identifying the costs of controlling risks and that the savings to be expected from a possible switch to direct management would be non-existent, because of the inevitable claims management and dispute monitoring operations.

5. From delivery to the country to transfer to the partners

79. Upon the arrival of goods in the recipient country, the country office takes control of the products, which are under WFP's responsibility at this stage.

80. Two schemes are possible: WFP handles storage and transport (through a contract with a transporter), and – in exceptional cases – direct distribution to beneficiaries. The field office delivers the goods to the cooperating partner responsible for storage and distribution.

5.1. Warehouses

81. In total,³⁴ as of the time of the audit, WFP used 871 warehouses, including 560 that it managed itself and 311 warehouses managed by a partner of the organization (governments, other agencies, private companies, etc.). WFP does not necessarily hold goods in all these warehouses at all times, and it can also store them elsewhere, particularly with vendors. As of 23 February 2018, WFP stored food in 357 warehouses managed by itself and 92 warehouses managed by WFP partners.³⁵

82. In addition to these warehouse figures, there are 70 airports, 680 ports, 237 containers located at transshipment points, and 110 vendors likely to have food stocks belonging to WFP.³⁶

Table 3: Number of warehouses managed by WFP and by partners of the organization in 2017*

Warehouses	871	Warehouses managed by WFP	560	Warehouses managed by WFP with food in stock**	357
				Warehouses managed by WFP with no food in stock**	203
		Warehouses managed by WFP partners	311	Warehouses managed by WFP partners with food in stock**	92
				Warehouses managed by WFP partners with no food in stock**	219

* These figures provide information only about warehouses where WFP food is stored before it is transferred to cooperating partners or beneficiaries.

** As of 23 February 2018.

Source: LESS extraction on WFP's food storage locations for 2017 (ZSCLSRSLC and ZSCOMINB extractions from LESS).

³⁴ ZSCLSRSLC and ZSCOMINB extractions from LESS.

³⁵ The "partners" referred to here are third parties and not WFP cooperating partners.

³⁶ Of this total, on 23 February 2018 food commodities were stored at 4 airports, 63 sea ports, 17 transshipment points and 20 WFP vendors.

83. For *storekeepers* in charge of WFP warehouses and storing food commodities,³⁷ an inspection of the building where the commodities are stored is expected to be performed at least once a week,³⁸ in addition to an inspection of the condition of the stored commodities. WFP also requires warehouses storing food commodities to be cleaned on a regular basis.³⁹ These inspections are intended to identify the general condition of the building where the commodities are stored in order to take any necessary action in the event of a proven danger of deterioration of the condition of the commodities.⁴⁰ WFP encourages warehouse managers to report these inspections in a book or form that must be made visible and available in the warehouse to keep track of changes in the conditions of the warehouse and the commodities from one inspection to another.

84. Warehouse inspections are carried out monthly in the case of warehouses managed by WFP third party partners and partners are expected to adhere to minimum standards of good warehouse management.⁴¹ However, the Warehouse Management Handbook and the instructions it gives are not included in the contract with the third party in charge of managing the warehouse and consequently are not binding on WFP partners. Similarly, a more extensive check is carried out by the country office on the management of warehouses by cooperating partners in the case of the food transferred to them by WFP.

85. Visits to the 10 field offices by the External Auditor revealed that the warehouses are generally well maintained. However, the frequent cases of non-compliance with the guidelines of the Warehouse Management Handbook raises questions about the type of warehouse supervision that WFP must do.

³⁷ The rules applicable to warehouse management are set out in The Warehouse Management Handbook (Handbook for Storekeepers of Food Aid"), http://home.wfp.org/manuals/op_warehousemgmt/English/about.htm.

³⁸ "Inspect the store and food stocks at least once a week so that prompt action can be taken if there are any problems", *Warehouse Management Handbook*.

³⁹ The floor must be cleaned every day, and the walls and shelves must be cleaned every week. Once a month, full cleaning of the warehouse must be done. If the warehouse is empty, it must also be fully cleaned.

⁴⁰ "Inspect the store itself for: leaking roof; broken windows or ventilators, badly fitting doors, cracked walls and floors, signs of entry of rats and mice. Inspect the outside of the store and the area around it", *Warehouse Management Handbook*.

⁴¹ See proposals of guidelines established by the United Nations Logistics Cluster (<http://www.logcluster.org/about-us>) and the document by the *Fritz Institute Certificate in Humanitarian Logistics Warehousing and Inventory Module* (used as a reference by UNICEF and WFP). See also Olsen D.R. (2003), *Gower Handbook of Supply Chain Management, 5th Edition, edited by John Gattorna, Gower*; Managan J., Lalwani C., et Butcher T. (2008), *Global Logistics and Supply Chain Management, John Wiley and Sons, Hoboken, New Jersey*.

Examples of warehouse visits

The Johannesburg office leases storage space in a Durban warehouse from a private company. Regional Bureau employees perform monthly inspections of this warehouse. The head of the supply chain unit goes there twice a year, and the person in charge of relations with this company goes every two or three months. The External Auditor noted the cleanliness and good organization of the warehouse, but found several quality risks. In particular, he noted that the contract with the manager did not include a clause formally excluding the storage of chemicals in the vicinity of the space leased by the office. The presence of chemicals (chromite and ammonium sulphate) in the same building, and some near food commodities, required verification at his request, which did not reveal any contamination. However, it had not been noted or reported by the co-contractor managing the warehouse.

The temperature in the warehouses was not systematically monitored, for example in the Harare, Masvingo, and Durban and Lilongwe warehouses. Yet, the handbook⁴² considers storage temperature control to be important: for all commodities – and not only those that specify specific storage conditions – overly high temperatures promote the deterioration of nutritional qualities as well as contamination by insects.

In the State of Palestine, the warehouse inspections carried out on behalf of the Jerusalem office revealed numerous instances of non-compliance with the guidelines of the Warehouse Management Handbook: storage of food commodities on the floor or against walls and non-compliant hygiene conditions.

86. Beyond a generally positive finding on the running of the warehouses visited by the auditors, the on-site WFP staff are often limited in number⁴³ and therefore unlikely to be able to closely monitor the service provider selected by contract, in order to prevent fraud, shorten time frames, and improve service quality. Similarly, the External Auditor found in Nepal that the office claimed to conduct regular inspections of its warehouses, but no trace was found of the visits having been planned or reported.

87. According to the country directors surveyed, the guarantee of effective performance of the outsourced activities is more based on sanctions, at certain key milestones during contracts (annual review of tenders, periodic suspensions of carriers, etc.), than on close control and frequent oversight of activities.

88. This policy based on ex post controls can lead to inertia as regards ongoing monitoring of the quality of performance of the contract. As the local private sector becomes stronger and is able to perform certain logistical activities more cost-effectively, the ability to take on an oversight role, while retaining the same level of efficiency, should henceforth be a key focus for WFP.

89. Contractual outsourcing does not obviate the need for proper oversight of performance, which, unless exercised by WFP with the appropriate resources, methods, and frequency, runs the risk of complete delegation, meaning that it is only possible to reduce risks in a later phase and off-site, or because it is fortuitously flagrant, as found in Mombasa.

⁴² Warehouse Management Handbook, “Chapter 2 – Stores Premises”, “Chapter 7 – Inspection of stocks and the store.”

⁴³ For example, in Kenya, a single employee, tasked with coordinating with the partner, in a facility capable of holding 30,000 mt of food.

An example of blatant fraud

The External Auditor witnessed blatant food diversion in Mombasa (Kenya) on 10 November 2017. A truck owned by a company contracted by WFP since May 2017 for transit and storage activities, knowingly passed a number of bags to third parties in the presence of the External Auditor and the Director of the Mombasa sub-office. The director noted this event and informed the company and the country office in Nairobi. At the request of the WFP office, the company in question suspended the driver and disciplined him. He will no longer be assigned to WFP missions upon his return. Furthermore, transit assignments will henceforth be escorted by the company in order to prevent transit-related risks.

90. This situation raises the question of the best method to ensure the quality of services: strong on-site presence (which involves a cost) or contracts providing for strong penalties in case of incidents. WFP would be advised to look at the possibility of increasing security and escort measures at its third-party service providers, in high-risk areas, when negotiating the contractual clauses of logistics contracts.

91. In addition to the type of warehouse inspection, the question of the consequences of these inspections arises. The findings of inspections are not consolidated at regional bureau or central level. Although it is not necessary to forward the inspection reports to the offices and headquarters, the principle of decentralization does not preclude the higher level (here the regional bureau) from supervising the frequency of inspections and the follow-up by the country offices.

92. The Secretariat has explained that control procedures are in place, but that their frequency depends on the risks identified, bearing in mind WFP's non-extensible means. The External Auditor does not dispute the existence of checks, nor that a risk-based strategy is appropriate. However, this approach should not exempt country offices from planning their warehouse checks, or regional bureaux from having a summary of dates on which these checks were carried out and the main anomalies detected and the way they were followed up.

Recommendation 5. The External Auditor recommends strengthening the control of warehouses: a) by inviting country offices to plan inspections based on a risk analysis; b) documenting and keeping records of the inspections conducted; c) organizing documented monitoring of the frequency of warehouse inspections carried out by country offices.

5.2. Cooperating partners

93. Distribution to final beneficiaries can be done by existing government structures, by non-governmental organizations (NGOs) or by WFP. WFP can take charge directly if NGOs are unable to manage implementation or if direct distribution is less costly. However, cooperating partners account for approximately 98 percent of WFP food distribution.

94. Relations between the country office and a cooperating partner are formalized in a field level agreement (FLA), with the aim of entrusting these partners with the custody and distribution of commodities.

95. The general conditions require the partner to report on and authorize WFP's departments to perform all verifications deemed useful. The cooperating partner is required to report any damage or loss suffered by the products attributable to it or its employees, subcontractors, or representatives.

96. **The External Auditor asked the department responsible for relations with NGOs for copies of several FLAs. It replied that these agreements, totally decentralized, are managed at the local level and that it could not provide such documents.** They are not available in digital format in COMET. In addition, an internal audit stressed that the regional bureaux' supervisory role regarding the application of FLAs was not defined despite the many difficulties encountered:⁴⁴

- recurring delays in finalizing and signing FLAs, with some partnerships starting before signing;
- inconsistent application of FLAs between different country offices;
- audit visits to partners by the country offices not conducted systematically or uniformly.

97. Given the critical role played by the partners in distribution and the shortcomings noted in the recent past that characterize the partnership agreements, WFP should consider establishing a centralized collection system for FLAs.

98. The External Auditor also recalls its recommendation 6 in the 2017⁴⁵ report on decentralization, which aims to clarify the role of the regional bureaux in supervising the field offices. Monitoring the performance of partnerships is undoubtedly a key aspect of this supervision.

Recommendation 6. The External Auditor recommends: a) centralized collection of the agreements entered into with the partners; b) making the performance of partnership agreements in the field a priority area of oversight implemented by the regional bureaux.

6. From distribution to final consumption

6.1. Distributions by partners

99. The cooperating partners must provide periodic reports on quantitative data relating to the project to the WFP country offices for entry into the COMET system. These reports include details of stocks of food products, physical inventory counts, losses, and distribution figures within the time frames indicated in the operations plan. Unless otherwise indicated in the operations plan, these food distribution reports must be provided each month and presented to WFP within thirty days from the end of each month of performance of the programme(s) concerned.⁴⁶

100. Country office staff are responsible for validating all data reported via distribution reports in COMET. The regional bureaux and headquarters do not conduct random checks to verify the accuracy of reports on distributions by cooperating partners. The distribution reports are not communicated to them. However, given the large number of distribution points for each country office, case-by-case monitoring can only be performed at the decentralized level.

101. Headquarters makes an effort to improve checks on the reliability of the distribution reports from cooperating partners. Apart from the regulatory guidelines issued by headquarters, the deployment of LESS and COMET systems have increased the possibilities

⁴⁴ Report AR/16/12 of October 2016.

⁴⁵ WFP/EB.A/2017/6-G/1.

⁴⁶ According to "Section C – Special Provisions on Reporting" of Annex 1-A – Food Distribution and Related Activities, *Field Level Agreement (FLA)*.

of monitoring food commodities, particularly by allowing data on deliveries (LESS) to be reconciled with those on distributions (COMET).

6.2. Feedback from beneficiaries

102. Headquarters does not deal with individual complaints and beneficiary comments (with the exception of the Office of the Inspector General, when matters are brought to its attention). This function is decentralized to the country offices (complaint and feedback mechanism). Headquarters tracks the number of countries that have mechanisms in place to collect complaints and, more broadly, feedback from beneficiaries (complaint and feedback mechanisms).

103. The main existing mechanisms for collecting feedback from beneficiaries are a hotline (free calls) and a help desk (whose participants are stakeholders: WFP, government, cooperating partners, local managers⁴⁷), and day-to-day interactions with the representatives of beneficiaries (who participate in field committees in the case of refugee camps). Post-distribution monitoring tasks allow opinions and complaints to be collected from beneficiaries.

104. **However, these mechanisms are not widespread or uniform. They are not integrated identically into the project cycles implemented at the country office level. The preliminary findings of the latest inquiry on the country offices' annual reports for 2017 indicate a ratio of country offices with a beneficiary feedback mechanism of 80 percent at the time of the audit.**

6.3. Risk of diversion after distribution

105. The COMET system records the quantity of losses and the reasons for losses, but it does not specifically include a search for data on illegal uses of food such as diversions, resales, and trafficking. Headquarters does not carry out any global analysis, in terms of volume or value, of this type of loss, which calls into question not only its effectiveness but above all its reputation.

106. The post-monitoring distribution questionnaires completed during assessments of the programme's effectiveness with partners and beneficiaries are based on qualitative surveys. They rarely address the issue of food diversion, focusing on diets, nutritional aspects, or household strategies to cope with food poverty.

107. The post-distribution monitoring tasks carried out by the field offices are sometimes performed by the cooperating partners themselves, which undermines the impartiality of the feedback. **The very strong social pressure observed in certain audited areas suggests that the beneficiaries will not denounce a partner NGO close to the government and responsible for distribution or the authorities themselves during a visit by a WFP employee.**

Recommendation 7. The External Auditor recommends: a) extending beneficiary feedback mechanisms to all regional bureaux; b) examining the possibility of strengthening the procedures for detecting illegal uses of distributed food.

⁴⁷ According to the rules provided for in the memorandum of understanding with the government.

7. Food safety and quality

108. The destruction of food products as a result of quality incidents amounted to USD 2.9 million for 3,532 mt. While the proportion of destructions of food commodities in the total food commodities handled remains marginal (0.13 percent of food commodities handled by value), the questioning of the quality of its food exposes WFP to humanitarian and reputational risk. The field offices are frequently exposed to such risks, inseparable from the nature of their mission.

7.1. Quality control system

109. There are three levels of risks associated with loss of quality of food commodities in the WFP food basket: low, medium and high, depending on the characteristics of the food commodities being channelled.

110. Before joining the pool of international WFP vendors, the organization ensures the quality of medium and high-risk food commodities, particularly processed products and specialized nutritious foods, by means of a quality assurance process based on questionnaires from candidate companies (initial paper assessment – IPA) and audits of factories. These audits are mandatory before companies join WFP's pool of international vendors. If there are any non-conformities, the company is required to put corrective measures in place within a specified time. Since 2014, WFP has audited all international vendors of specialized nutritious foods it draws upon, totalling 166 in 2017. To date 59 companies have been audited, i.e. less than half of vendors.

111. Contract surveyors also undergo quality tests at the time of taking possession of food commodities for WFP, during which the quality, nutritional value and risk to beneficiaries' health – according to the contractually agreed specifications – are verified. At the end of the supply chain, WFP performs tests on the nutritional value of food commodities and the storage duration of processed products and specialized nutritious foods, according to a calendar planned at the start of the year depending on the risks identified over the course of supply. These tests are performed with the support of private sector funding.

7.2. Quality control limits

112. The two main causes of food losses in 2017 were transport and storage duration (see Table 2). **WFP must make decisions between the storage of food as close as possible to recipients who live in troubled areas and the resulting risks of looting.** These risks materialized, for example, in South Sudan, with the theft of 4,500 mt in 2016 and 660 mt in 2017.

113. The Food Quality and Safety Unit (OSCQ) acts as an expert at the request of the field offices and other departments. It arranges the analysis of defective products reported to it. It is informed of these incidents either by referral to a country office or by the procurement unit at headquarters. It does not receive quality surveyors' reports directly, unlike the procurement unit at headquarters. The reports are sent to the procurement unit, which then assesses whether it is appropriate to communicate them to OSCQ. This separation of tasks raises a question of principle, since it is up to the buyer, who is contractually bound to the supplier and who does not necessarily have knowledge in quality monitoring, to refer the matter to the appropriate unit.

114. All in all, this unit does not systematically monitor quality incidents, contrary to an internal audit recommendation. A budget is under consideration to fund an information system compatible with LESS and COMET for this purpose.

115. The audit on the Kenya office revealed that the reporting of incidents by country offices is limited to recording in LESS and communication by email in case of a major incident. The standardized "*Rapid Incident Notification Grid*" (RING) template, created to enable headquarters to track these incidents, remains unfamiliar to field staff. The audits of the Zimbabwe office and the Cairo Regional Bureau led to a similar finding. For the first time, quality training courses are planned for field office staff. The first training course took place in February 2018 in Ethiopia.

Recommendation 8. The External Auditor recommends strengthening internal quality control: a) by forwarding all inspection reports to the Food Quality and Safety Unit (OSCQ); b) by establishing an exhaustive information system on quality incidents allowing OSCQ unit to perform monitoring and management; c) by continuing the deployment of the quality assurance system in order to reduce the organization's dependence on one-off product inspections.

8. Information systems

116. **Two systems coexist to track food commodities. WFP does not have an integrated tool for monitoring food commodities along the supply chain.**

117. LESS tracks all movements until transfer to partners in near-real time. Entry is not automatic and requires human operation; differences of several days or more were found between the tracked event and its entry into LESS.

118. LESS is not continuously updated upon the arrival of new loads, but once the customs and administrative formalities have been dealt with. At the Durban (South Africa) warehouse, for example, we saw thousands of sacks of wheat that were not in the warehouse manager's inventory and were therefore absent from LESS. The presence of this wheat load had not yet been entered into the system because repackaging and a customs validation were pending.

119. The audit of the Johannesburg Regional Bureau revealed a 68 mt difference in vegetable oil stocks between the warehouse management company's inventory as of 31 October 2017 and the figure extracted from LESS for the same date. After several searches, it appeared that this discrepancy corresponded to two loads that could not be recorded in LESS (because of a technical problem).

Recommendation 9. The External Auditor recommends striving for real-time data recording in LESS in order to set up this system as a true food commodities tracking system.

120. WFP's second information system is COMET (country office tool for managing effectively), which was designed to monitor operations, programme design, and performance of operations conducted by WFP cooperating partners.⁴⁸

121. COMET contains important programme management documents, and a database of performance indicators for WFP activities. The system lies at the heart of the framework of institutional results for 2017–2021, which links country office activities to sustainable development goals (SDGs).

122. Country offices are responsible for entering information in COMET. This information is not totally uniform from one office to another on account of varying use of COMET, particularly as regards dates of entry of data into the system.

123. The information, as entered and processed on the system, is not always usable for headquarters teams. On request from the Supply Chain Division (OSC), information on the reasons for losses suffered during food distribution have been improved. The fact remains that the consolidation of data on losses in COMET is not always carried out in response to losses, as requested by OSC, but by batches, rendering the information on losses suffered difficult for logistics teams to use, and they may be led to process a file combining various types of unrelated loss.

9. Valuation of losses

124. Losses are tracked in near-real time in LESS and are accessible via INFOHUB globally and by country. They are analysed in terms of volume and value according to several criteria: causes, products, regional bureaux, country, and period.

125. Field audits have shown that there is no uniform perception among WFP employees of what a food loss is. The departments have an understanding of it that depends on their use of it.

126. Losses tracked in the LESS system therefore correspond to the reference food valuation mode as defined in the WFP manual on applying the International Public Sector Accounting Standards (IPSAS).⁴⁹ The recording of the value of losses is automated, and the calculation is performed by an algorithm that calculates a moving average price or weighted average of the cost of food losses according to their purchase cost, all transport costs, and additional costs associated with repackaging the commodities in particular (fumigation, bagging, grinding, etc.). This loss valuation method is used as a reference for WFP staff for recording in LESS, the Finance and Treasury Division for Financial Statements, and the Operations Services Department for the post-delivery losses report (PDL).

127. The second approach corresponds to the loss valuation method offered by the 'Invoice' module, also in LESS, which aims to determine the amount of losses that must be deducted from the co-contractor's invoice. The value of losses here corresponds either to the price of the food defined by the purchase order or to the price of the food on the market at the arrival

⁴⁸ "Structure and Functionality of COMET", Directive "Use of COMET". Resource Management Department. 12 April 2016. RM2016/004.

⁴⁹ "The cost of food commodities includes purchase cost or fair value if donated in-kind and all other costs incurred in bringing the food commodities into WFP's custody at their point of first entry into a recipient country where they become distributable. In addition, any significant costs of conversion such as milling or bagging are included. Cost is determined on the weighted average basis". WFP Policy Guidance Manual for IPSAS.

point plus transport costs and additional costs.⁵⁰ Unlike the previous approach, the calculation is not an average here. The choice between the alternative price of the commodity at the time of purchase or on the market is left to the country office, the aim being to pass on the higher cost on the co-contractor's invoice. In this way, WFP limits the risk of co-contracting parties reselling the food at market price above that offered by WFP at the time of food commodity procurement.

128. Lastly, the third method is the valuation of losses as specified in the insurance declaration signed by WFP for each shipment. It is obtained by adding the price of commodities as specified in the purchase order plus the cost of maritime freight plus the weighted average of costs associated with routing to the final delivery point or LTSH costs (landside transport, storage and handling). It is used for WFP claims for losses of insurable commodities. As this valuation method only applies to losses incurred by WFP shipments in the pre-delivery phase,⁵¹ it does not include ground transportation costs after delivery or ITSH costs (internal transport, storage and handling).

129. None of these definitions is formally inaccurate, as each corresponds to a particular usage. However, it should be noted that the application of these three methods to the example of a truck theft whose cost was charged to the operator of a warehouse leads to a 20 percent difference between the two extreme figures.⁵²

130. The valuation configured in LESS, which serves as an official inventory of losses, could be less than the valuation based on actual costs and invoiced to the co-contractors or even the valuation that results in compensation.

131. The method WFP uses to value its losses in the financial statements can be considered compliant with applicable accounting standards and the WFP manual.

132. Without wishing to question this accounting policy, the External Auditor believes that, in the case of values tracked in LESS, which is an operational tool, WFP might want to consider a method based on real values and not weighted averages.

V. ACKNOWLEDGEMENTS

133. The audit team wishes to thank the Supply Chain Division (OSC) and the Finance and Treasury Division (RMF), who were all called upon.

End of audit observations.

⁵⁰ "All missing or damaged commodities and any excess spillage or leakage during the period under your responsibility will be debited against transport invoices based on the arrived commodity value or the market value at final destination, whichever is greater. The arrived value at destination is calculated by adding all transport and related costs to the value of commodity". Transport Manual, Section 5.3.3. – Overland Transport – Pre-Delivery Losses.

⁵¹ Up until application of the extension of coverage proposed to the Executive Board.

⁵² Example drawn from the audit of the Johannesburg Regional Bureau. LESS: USD 30,282; Invoice: USD 34,200; Operational Risk Management Service (OSCR): USD 36,238.

APPENDIX 1 - Approximation of complete costs of losses in 2016 and 2017⁵³

Losses	(a)	(b)	(c)	(d)	(e)	(a)	(b)	(c)	(d)	(e)
	2016					2017				
	Losses by volume (mt)	Losses by value (USD)	Reductions in vendor invoices	Claims paid to WFP	Real losses (USD)	Losses by volume (mt)	Net losses by value (USD)	Reductions in vendor invoices	Claims paid to WFP	Real losses (USD)
Pre-delivery	10,791	6,084,737	2,977,054	3,275,710	1,816,676	11,199	5,939,588	3,695,082	9,896,029	- 5,188,135 (1)
Post-delivery	17,441	16,092,946		x	15,100,595	13,599	12,125,078		x	10,893,384 (2)
During distribution	2,668	1,977,991		x	985,640	3,679	2,473,338		x	1,241,644 (3)
Post-distribution	x	x	x	x	x	x	x	x	x	x
Total	30,900	24,155,674	2,977,054	3,275,710	17,902,910	28,477	20,538,004	3,695,082	9,896,029	6,946,893
Premiums paid by WFP to the Captive insurance					6,217,921					6,130,785
Premiums paid to Re-insurer (Captive insurance)					452,734					561,278
Premiums paid to external insurer (Bilateral Shipments)					166,789					43,992
All costs associated to losses					24,740,354					13,682,947

⁵³ (1) 2016: $6,084,737 - 2,977,054 \times \frac{1}{3} - 3,275,710 = 1,816,676$; 2017: $5,939,588 - 3,695,082 \times \frac{1}{3} - 9,896,029 = - 5,188,135$; (2) 2016: $16,092,946 - 2,977,054 \times \frac{1}{3} = 15,100,595$; 2017: $12,125,078 - 3,695,082 \times \frac{1}{3} = 10,893,384$; (3) 2016: $1,977,991 - 2,977,054 \times \frac{1}{3} = 985,640$; 2017: $2,473,338 - 3,695,082 \times \frac{1}{3} = 1,241,644$.

Key: Reductions in vendor invoices for losses imputable to them (column c) are deducted from losses recorded in the LESS finance module (column b). These invoice reductions may take place at three stages of supply of food commodities. The External Auditor therefore subtracted third-party losses by value from total invoice reductions obtained by WFP for each line concerned. From the first line ("Pre-delivery losses) compensation paid to WFP by the Captive was also deducted, intervening in 2016 and 2017 only at that stage of the supply chain.

Acronyms used in the document

COMET	country office tool for managing effectively
FLA	field level agreement
IPSAS	International Public Sector Accounting Standards
ISSAI	International Standards of Supreme Audit Institutions
LESS	Logistics Execution Support System
NGO	non-governmental organization
OSC	Supply Chain Division
OSCQ	Food Quality and Safety Unit
SDG	Sustainable Development Goal
WINGS	WFP Information Network and Global System