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**Executive Board  
Second Regular Session**

**Rome, 22–26 October 2007**

# **RESOURCE, FINANCIAL AND BUDGETARY MATTERS**

**Agenda item 5**

*For consideration*

# **E**

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## **SPECIAL AUDIT REQUESTED BY THE EXECUTIVE BOARD IN RELATION TO WFP'S ACTIVITIES IN THE DEMOCRATIC PEOPLE'S REPUBLIC OF KOREA**

**Report by the External Auditor**

## NOTE TO THE EXECUTIVE BOARD

**This document is submitted to the Executive Board for consideration.**

The Secretariat invites members of the Board who may have questions of a technical nature with regard to this document to contact the WFP staff focal points indicated below, preferably well in advance of the Board's meeting.

Director, Office of the External Auditor:    Mr G. Miller            tel.: 0044 2077987136

External Auditor:                                    Mr R. Clark            tel.: 066513-2577

Should you have any questions regarding matters of dispatch of documentation for the Executive Board, please contact Ms C. Panlilio, Administrative Assistant, Conference Servicing Unit (tel.: 066513-2645).





## International Audit

The National Audit Office (NAO) provides external audit services to the World Food Programme. The External Auditor, Sir John Bourn, has been appointed by the Executive Board in accordance with Article XIV of the Financial Regulations. In addition to providing an opinion on the financial statements of the WFP, he has authority under the mandate to report to the Executive Board on the efficiency of the financial procedures and the general administration and management of WFP.

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

The aim of this report is to respond to the request of the Executive Board for a special external audit in relation to Programme operations in the Democratic People's Republic of Korea.

# External Audit Report to the Executive Board

## World Food Programme

### Special audit requested by the Executive Board in relation to WFP's activities in the Democratic People's Republic of Korea

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## EXECUTIVE SUMMARY

1. In February 2007, in response to questions raised regarding United Nations operations in the Democratic People's Republic of Korea (DPRK), the UN Advisory Committee on Administrative and Budgetary Questions (ACABQ) asked the United Nations Board of Auditors to carry out a special audit on the operations of the UN organisations, including the UN funds and programmes, in the DPRK which fall within the Board's mandate. The scope of the work requested focused on compliance with applicable financial regulations and rules, accountability frameworks and other directives, as well as to ensure that money expended in DPRK went to the intended recipients. The areas to be reviewed included foreign currency transactions, staff hiring, access to reviewing local projects and their outputs, and direct payments for national execution projects.
2. The World Food Programme's Financial Regulation 14.6 provides that the WFP Executive Board may request the External Auditor to carry out specific examinations and issue separate reports thereon. In February 2007, the Board requested a special external audit of WFP operations in the Democratic People's Republic of Korea (DPRK)<sup>1</sup> emphasising the need to consult and coordinate with the United Nations Board of Auditors special audit of the same issues relating to other United Nations funds and programmes. Annex 1 refers.
3. By letter dated 29 March 2007 to the President of the Executive Board, the External Auditor, the Comptroller and Auditor General of the United Kingdom, confirmed that we would carry out the special audit as requested. Annex 2 refers. We undertook to report back to the June 2007 meeting of the Executive Board, if necessary as an interim report, orally or in writing. In accordance with our interim oral report to the June Board and after consideration of the report of the United Nations Board of Auditors in relation to other UN organisations, this report now presents the findings of our examination.
4. Prior to these issues being raised and the Executive Board's request for a special audit, we had already visited WFP's country office in DPRK in September 2005. Our management letter to the Secretariat in December 2005 on our DPRK audit visit set out 16 recommendations and included key audit findings on the recording and disclosure of transactions as emergency operations which had the characteristics of a protracted relief and recovery operation or development activity; control risks and inadequacies arising from limitations the government placed on field monitoring activities and the lack of unrestricted access to beneficiaries, adversely affecting the level of assurance available over the integrity of monitoring; and under-reporting of post-delivery losses of food. We also covered these issues in our reporting to the EB on post delivery losses (February 2006) and in our financial report on the 2004-2005 financial statements (June 2006).

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<sup>1</sup> 2007/EB.1/8

5. In response to the Executive Board's specific request, we carried out a review and update of the findings from our previous visit to DPRK and additional work in Headquarters to assess WFP's position in the light of the concerns expressed by the Advisory Committee on Administrative and Budgetary Questions, embodied in their request to the UN Board of Auditors for an examination of the operation of UN Funds and Programmes in DPRK.

6. Our review of the situation after late 2005 considered the extent of currency exposure of WFP inside DPRK by considering the nature and significance of WFP's DPRK emergency operation (10141.3). The authorised budget for this project included food deliveries costing US\$129 million and other costs amounting to US\$74 million. 63 per cent of the project budget provided for expenditure on food rather than as hard currency payments to DPRK. Of the cash-based expenditure, staffing costs included 47 international staff whose salary would be paid mainly external to DPRK. Project expenditure had amounted to only US\$22.7 million by March 2007. These factors have served to reduce the extent to which WFP's activities have imported foreign currency to DPRK other than in payments to staff.

7. There has been a significant reduction in WFP operations in DPRK in 2007. In 2006, WFP agreed with the DPRK Government on the implementation of a protracted relief and recovery operation to replace emergency operations from June 2006; and as at May 2007, WFP's accounting system recorded some US\$23 million of resource income, representing only 22 per cent of the budget of the two-year project life span to March 2008.

8. Under similar arrangements to those operated in DPRK since 1996, the National Coordinating Committee and the General Service Bureau of the Government provide all national employees to WFP as Government secondments rather than employees. This has imposed clear constraints on WFP in the selection and appointment of staff. However, WFP's allocation of management responsibilities has mitigated the risk of undue influence from Government-supplied national staff or of inappropriate management or unsupervised reporting responsibilities being undertaken by staff provided by the Government under the terms of the partnership agreements.

9. As a result of this further audit review, we provide six recommendations aimed at:

- More effective response to risk and oversight, including audit outputs;
- Effective maintenance of equipment supplied to factory units currently on standby;
- Ongoing allocation of key financial and programme management responsibility to WFP-appointed staff;
- Cost-effective and secure currency arrangements for payments;
- Strengthening of field monitoring arrangements confirming food delivery; and
- Robust reporting of post delivery loss and consignment deliveries.

## BACKGROUND AND SCOPE OF AUDIT REVIEW

10. On 25 January 2007 the United Nations Controller, Mr Warren Sach, wrote to the Chairman of the Advisory Committee on Administrative and Budgetary Questions (ACABQ) to request a United Nations Board of Auditors examination of the operations of the United Nations Funds and Programmes in the Democratic People's Republic of Korea, following the United Nations Secretary General's call for an urgent external inquiry into the activities of the United Nations funds and programmes.

11. The UN Secretary General indicated that his request for a special audit of DPRK should be a UN system wide review to focus on:

- Past and current compliance with the applicable Financial Regulations and Rules, accountability frameworks and other directives;
- Foreign currency transactions;
- Staff hiring;
- Assurance that resources expended in DPRK went to the intended recipients;
- Access to review of local projects and their outputs, and
- Direct payments for projects undertaken by national authorities.

12. WFP General Rule XII.1 requires recipient governments to give full cooperation to enable authorised personnel of WFP to monitor operations. To examine the effectiveness of monitoring, we considered the access to beneficiaries and monitoring procedures to address two of these concerns in relation to WFP - assurance that resources went to the intended recipients and access to review of local projects.

13. Some international press coverage referred to other concerns related to UN organisations, such as:

- Cash payments in hard currency and counterfeit United States currency held by UN organisations (addressed under foreign currency transactions);
- Government-nominated staff controlling UN activity by performing financial and programme management functions (addressed under staff hiring); and
- Equipment being provided to DPRK (considered under compliance with applicable financial regulations and foreign currency transactions).

14. Under its authority in Article VII of the United Nations Financial Regulations and Rules, in a letter dated 9 February, ACABQ asked the Board of Auditors to carry out as a matter of priority a special audit of the operations of UN organisations in the DPRK, and to report its findings to the Advisory Committee. The letter recognised United Nations Development Programme (UNDP) as the lead agency but noted that the Board of Auditors might wish to consult the auditors of other UN entities. In his capacity as Chairman of the Board of Auditors, Mr Philippe Séguin, Premier Président of the Cour des Comptes, responded to the ACABQ request on 22 February 2007, confirming that the Board of Auditors would undertake the audit. The Board of Auditors subsequently issued its report to ACABQ dated 31 May 2007.

15. Subsequently, the WFP Executive Board asked us, under Financial Regulation 14.6, to carry out a special external audit of WFP's operations in DPRK. This request recognised, and we emphasised, the need to co-ordinate our approach with our colleagues from the UN Board of Auditors, to assist in examining any areas of concern in relation to WFP arising from the global findings; and to avoid any implication that WFP operations represented more urgent or significant risk than those addressed by our audit colleagues.

16. This present report now sets out for the WFP Executive Board our audit findings, and our recognition of the Board of Auditors' findings and conclusions, in so far as these have relevance to the context of WFP's operations in DPRK. We also provide where appropriate our analysis of the amounts spent by WFP, to assist the Executive Board in assessing the context in which the concerns expressed about other funds and programmes are relevant to WFP operations.

17. Our reports to the EB have raised issues and recommendations arising from field visits, including DPRK. Progress against our recommendations is reported to every EB until the Secretariat deems the response to be complete, after which we provide comment on the completed recommendations. Following our audit visit to DPRK in late 2005, we reported specific concerns:

- Our post delivery losses report to the Board in February 2006 reported weaknesses in the monitoring of food losses, drawing on our DPRK findings and making recommendations for improved monitoring and reporting;
- Our financial report to the Board in June 2006 raised the matter of outstanding issues and balances with UNDP, with a recommendation to WFP to reconcile the inter-agency accounts. The WFP Audit Committee had supported our request for a note of explanation of outstanding items to be included in the 2004–2005 statements prior to giving our audit opinion; and
- The risk analysis in our programme of work provided to the November 2006 Board referred to risks associated with reliance on implementing partners, post delivery loss reporting and a reputational risk associated with the use of third parties to meet corporate objectives. We undertook to continue reviewing the robustness of implementing partner reporting.

18. Following the EB's request for a special audit, we updated our findings from late 2005, taking account of management's responses to our management letter; and carried out further work from Headquarters to more directly address the specific concerns raised. In particular, we:

- Reviewed in the current context previous reports by Oversight Services Division on internal audit of WFP operations in DPRK (in 1997 and 2004), and our predecessors' report of their external audit visit in 1999;
- Requested and reviewed information and analyses from the WFP Country Office in DPRK;
- Analysed WINGS and project database records;
- Reviewed vendor data;
- Discussed issues with WFP Operations staff;
- Examined the WFP-UNDP memorandum of understanding agreed in May 2007; and
- Reviewed the letter of understanding and arrangements between WFP and DPRK in relation to current activities.

19. This report now provides findings and recommendations in the context of the key areas which have been the subject of concern:

- Accountability frameworks;
- Compliance with applicable financial regulations and rules;
- Staff hiring;
- Foreign currency transactions;
- Access to beneficiaries and monitoring procedures; and
- Direct payments for projects undertaken by national authorities.



## ACCOUNTABILITY FRAMEWORK

20. Under financial regulation 3.1, the Executive Director is responsible and accountable to the Board for the financial management of the activities of WFP. Oversight of this management activity by the Executive Board is facilitated by the Secretariat's reporting to the EB and complemented internally by the Oversight Services Division and the Audit Committee. External oversight is provided by the External Auditor, governed by Article XIV of the financial regulations.

21. The Oversight Services Division carried out internal audits of the DPRK Country Office in 1997 and 2004. The aims of the 2004 audit were to consider Country Office compliance with WFP rules, regulations and formal guidance; review internal control structures and the regularity of transactions; verify the completeness and accuracy of accounting records; examine procedures for safeguarding assets and the economic and efficient use of resources. We refer to the findings of these visits where appropriate in this report, and in particular the comments and actions subsequently taken by the Secretariat, but the internal audit raised 62 recommendations, nine of which were classified as significant, against findings of, for example:

- The Country Office working in a restrictive environment not conducive to the effective and efficient running of its operations.
- Government prohibition of random monitoring access and difficulty in obtaining information to allow WFP to ensure that food resources are properly utilised.
- Internal control weaknesses relating to procurement.
- Insufficient information/documentation to support short listing of suppliers and absence of periodic review of suppliers' performance.
- Unsupported and un-evidenced cost sharing arrangements with UNDP.

22. We visited and reported by management letter to the Secretariat on DPRK operations in September 2005 as part of our regular programme of field visits to WFP country offices and regional bureaux. These visits support our biennial audit of the financial statements and result in management letters (reports to management) after each visit. These reports to management are also communicated to the Audit Committee. We separately report to the Executive Board (EB) through subject-based reports on management topics and, at the end of the financial period, on the results of our programme of work generally.

23. In our visits to country offices, we review risks associated with WFP's decentralised worldwide activities including financial oversight and compliance with regulations and rules. Prior to each visit we carry out a risk assessment which aims to cost-efficiently focus audit attention on areas which may be of higher risk, including examination of the operating environment and previous audit reports; involves discussion with

regional and Headquarters financial and operational managers; and analytical review of country project transactions.

24. Our visit examined risk areas outlined in previous WFP audit visits including financial oversight, compliance with regulations, limitations on the monitoring of food delivery, staff hiring, and payments to other UN organisations or to government ministries. Our report to management raised 16 recommendations, 14 of which were assessed as high or medium priority, concerning for example:

- Inappropriate classification of programme activities.
- Procedures that adversely affected the level of assurance and integrity of food monitoring.
- Unrecorded and incomplete post delivery losses of food, in a context of inadequate monitoring arrangements.
- Incorrect postings in the WFP WINGS accounting system.
- The absence of regular verification of non-consumable inventory.
- Absence of prompt invoicing for services provided.
- Un-reconciled transactions and balances with UNDP.
- Cost-sharing with UNDP unsupported by proper contractual arrangements.
- Long standing receivables in open vendor and staff advances.

25. In a decentralised structure, the effectiveness of management oversight from Headquarters represents a key element in the system of internal financial controls. Given that by 2006 WFP had benefited from both internal and external audit of operations in DPRK, in order to avoid unnecessary exposure to the sort of concerns raised by ACABQ and others, it is important for management to ensure that appropriate action is taken in response to audit recommendations. In a decentralised organisational structure, it is especially important that audit findings are used effectively to inform assessments or re-assessments of risk and operational practice and procedure.

***Recommendation 1: We recommend that the Secretariat ensure the maintenance of:***

- ***Timely and adequate response to internal and external audit recommendations; and***
- ***Robust risk assessment of country office operations.***

## COMPLIANCE WITH APPLICABLE FINANCIAL REGULATIONS AND RULES

### Procurement

26. Management control over procurement in DPRK relies on compliance with WFP's standard procurement rules and procedures.

27. In 2004, DPRK had the largest aggregate value of procurement activity in the Asia Region. Local suppliers hand carried or mailed their quotations while overseas suppliers submitted quotations by fax, mainly from China. An audit report by WFP's Office of Oversight Services (internal audit) released in July 2004 drew attention to the absence of confidential fax facilities, the lack of an opening panel for quotations and no periodic evaluation of supplier performance. The report also noted inadequate documentation of the reasons for rejection of suppliers on financial grounds. Following the audit, the Country Office confirmed the establishment of confidential faxing facilities for incoming quotations; reinforced performance evaluation of suppliers; and enhanced the documentation of reasons for vendors being rejected on financial grounds.

28. Our latest examination of DPRK vendor listings of suppliers and staff, comprising 232 vendors, confirmed that 130 were based in DPRK and 68 in China. In general, major procurement of non-food items had been made through the Beijing liaison office. The Secretariat confirmed that local purchases are subject to a competitive tender process, with payment of those above the petty cash limit of €50 (US\$ 67) being actioned through purchase order.

### Nature of programme activity

29. WFP rules and regulations, including Secretariat funding authorisations, vary according to the nature of programme activities. Therefore an accurate and consistent approach to designating programmes is important to ensure compliance with the appropriate rules.

30. Our audit visit to DPRK in 2005 had revealed that the Country Office charged activities to an emergency operation (EMOP 10141.3) even though the programme more closely conformed to the definition of either a protracted relief or recovery operation (PRRO) or a developmental activity. For example of 491,741 metric tonnage of food planned for distribution in 2005, 127,920 metric tonnes (26 per cent) were to be distributed to organisations generally associated with emergency feeding projects - orphanages, the elderly and urban poor. The remaining 363,821 metric tonnes (74 per cent) were planned for distribution to organisations usually supported by PRRO projects such as nurseries and schools.

31. Further, WFP had supported the opening of 19 local food production factories across DPRK since 1999: an activity more characteristic of development than emergency operations. One state-owned manufacturing plant in Pyongyang which we visited in 2005 produced WFP biscuits for distribution to beneficiaries. WFP provided packaging materials for the biscuits and spare parts for the machinery in addition to the biscuit ingredients. In May 2007, only seven of these factories remained in operation as a result of the reduced

support available under the new PRRO. The equipment provided by WFP for these standby factories remained under the ownership of WFP with current agreements allowing a visit to factories once every two months.

32. The Secretariat confirmed that the definition of the nature of activity had been a major concern for a number of years. As early as 2000, negotiations with the Government and donors to implement a PRRO project proved unsuccessful and an EMOP remained the preferred instrument to provide food aid to the beneficiaries. Following our visit, the WFP Executive Board<sup>2</sup> in February 2006 approved PRRO 10488.0 for two years (2006–2007), endorsed by the subsequent signing of a Letter of Understanding between WFP and DPRK on 10 May 2006.

33. In 2007, after the departure of the final UNDP staff from DPRK following suspension of UNDP activities, a Memorandum of Understanding between WFP and UNDP made WFP caretaker of UNDP assets. The Memorandum required WFP to periodically visit UNDP premises to inform UNDP of the status of assets remaining on the premises and generally protect UNDP's interests. Payment from UNDP was agreed at direct cost recovery plus a four per cent management fee.

34. In these respects, the funding and nature of WFP's DPRK programmes have been reported and approved in accordance with financial regulations at the relevant Executive Board meetings.

***Recommendation 2: Although we welcome the clarification of the nature of operations in DPRK, we encourage the Secretariat to ensure the effective maintenance of equipment supplied to factory units currently on standby. Where standby factories are deemed unlikely to be reopened, WFP equipment should be cost-effectively recovered or transferred to the Government partner in accordance with the financial rules at the end of the programme to avoid any unforeseen risks to WFP.***

## STAFF HIRING

35. Under similar arrangements to those operated in DPRK since 1996, the National Coordinating Committee and the General Service Bureau of the Government provide all national employees to WFP (and other UN entities) as Government secondments rather than employees. Since the latest project agreement in 2006, the Government provides two or more candidates to WFP for interview for national officer vacancies. While the training and experience currently gained by national staff supplied by the Government appears to be in accordance with the project's stated aims of assisting the longer-term development of

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<sup>2</sup> 2006/EB.1/16

sustainable food supply and progressive reduction in food aid, this represents a clear constraint on WFP over the selection and appointment of staff.

36. At the same time, our examination yielded reasonable assurance that the Secretariat had implemented a management control environment covering such secondments. Although some of these staff maintained financial records, our examination confirmed that:

- Final authorisation or certifying officer responsibilities had been allocated only to WFP international staff; and
- National staff did not have access to the accounting software in WINGS after its introduction into DPRK in 2002.

37. We examined expenditure on staffing provided to the Government over the seven-year period from 2000 to 2007. Annex 3 to this report provides a year on year analysis of payments to the Government and directly to seconded staff, amounting to US\$3.5 million and showing that:

- Total payments to Government agencies amounted to US\$850,331 for local staffing; and
- Direct payments to seconded staff totalled US\$2.7 million, of which US\$1.8 million arose from the costs of local travel including subsistence allowances.

38. In 1999, the External Audit report following our predecessors' visit to DPRK revealed delays in excess of three months in the recruitment of core international staff. The report emphasised the need for the Secretariat to ensure that no unfilled posts existed in management and financial positions. Following the report, we found no evidence of significant delay in filling financial or management posts. In May 2004, 47 international staff and 70 local staff had been in post. In April 2007, the Country Office employed ten international staff and three locally recruited international officers.

39. In early June 2007, DPRK authorities informed WFP that it should stop employing locally recruited international staff at the beginning of July 2007. These staff had traditionally worked in finance and administration under the supervision of the Finance Officer. At the time of our review, the Country Office was discussing with the authorities the possibility of retaining at least those staff who were spouses of staff from other UN organisations in DPRK. WFP have informed us that the Government has agreed to permit the employment of qualified UN spouses on locally recruited service contracts.

## Exit strategy

40. Our management letter from 2005 recommended that the Secretariat should have an exit strategy in place to ensure the availability of funding and an adequate agreement between the partnerships. The current programme sets out a time frame of five to ten years during which the Government would continue to implement measures to restore food security, but would require commercial imports and aid. Depending on circumstances, the programme envisages a progressive reduction in the amount of food assistance meeting immediate needs together with longer-term development to support the Government's efforts.

**Recommendation 3: We recommend that the Secretariat continue to make international staff responsible for all financial and programme management and wherever possible to restrict access to the accounting system to staff recruited by WFP.**

## FOREIGN CURRENCY TRANSACTIONS

41. Concerning hard currency payments to staff or Ministries, such payments arise in the normal course of activities at WFP in field offices we have visited. The rate of exchange in which the transactions are recorded to the accounting records is circulated each month by the United Nations and any foreign exchange loss or gain recorded.

42. Our examination revealed that from 31 May 2005 to 1 June 2006, the Country Office made 1,853 Euro cash payments amounting to €950,406 (US\$1.14 million). The Secretariat informed us that €2 million (approximately US\$2.5 million) had been brought into DPRK in 2006, of which €1.7 million (US\$2.1 million) had been expended. €1.3 million (US\$1.6 million) of this related to payment of the fuel subsidy to the Government to enable food transportation.

43. We confirmed that, to reduce the extent of cash payments made previously the Office had phased out Euro cash payments from June 2006, after which they were replaced by cheques cashable through the banking system. WFP maintains two DPRK-based bank accounts, one in DPRK Won and one in Euros with a combined balance equivalent to US\$6,640 at the end of 2006. A petty cash account holding €750 (approximately US\$1,024) is managed by an international finance officer with payment restricted to €50 (US\$68) for each transaction.

44. We confirmed that all United States dollar holdings and payments had been discontinued in 2002 after agreement with the Government that in future the Euro and Won would be the internal functional currency for operations. From February 2007, the Office had phased out Euro payments to local suppliers replacing payment in convertible Won. From May 2007 payments to Government Ministries for internal transportation of food will also be made in convertible Won rather than Euros.

45. We consider there has been a reduction in the risk of improper foreign exchange transactions from the decrease in cash payments, the introduction of payment through banks and the use of convertible Won for payment of suppliers. Our examination of other payments made to or on behalf of the Government which could involve foreign currency or value transfer revealed that:

- WFP had supported one study tour of a five-member delegation from DPRK in 2006, at a cost amounting to €17,000 (approximately US\$23,120) which formed part of development activity;
- Equipment supplied to the Government between 2000 and 2007 amounted to in excess of US\$560,000, analysed year on year in Annex 3 to this report.

46. The standard practice for disposal of equipment at the end of a WFP project is to transfer ownership to the Government partner. Our examination of the procedures for equipment transfer confirmed that regular meetings of the Local Property Survey Board (LPSB) have taken place over the period from 1998 to date. The LPSB has responsibility for advising the Country Director on the compliance of proposals for equipment inventory transfer with relevant procedures, rules and regulations. Our review of documentation related to the transfer of a truck valued at US\$39,721 to the Flood Damage Rehabilitation Committee in 2004 confirmed that management oversight and LPSB authorisation had been completed and evidenced.

***Recommendation 4: We encourage the Secretariat to minimise the risk of foreign exchange loss by maintaining efforts to ensure that payments reflect the most cost-effective currency arrangements; that cash payments are minimised; and that foreign exchange rates agreed with local vendors or Government Ministries are determined by the United Nations' monthly published rates of exchange.***

## ACCESS TO BENEFICIARIES AND MONITORING PROCEDURES

47. In 2005, we found evidence of the inadequacy of monitoring operations because of limitations imposed by DPRK authorities on WFP's access to beneficiaries. Audit observation of two food monitoring visits at a sub-office identified procedures that adversely affect the level of assurance available over the integrity of the monitoring operation:

- The DPRK Government required advance notice of planned food monitoring visits;
- WFP monitors were not provided with unrestricted access to field operations, limiting the assurance obtained over the type of beneficiary and the quantities of food consumed; and
- Interviews were conducted by non-Korean speaking WFP staff through an interpreter in the presence of government officials.

48. The Secretariat confirmed that limited access and monitoring had been a continuous concern over a number of years. The constraints placed on independent monitoring by WFP reduce assurance that food has been provided to the intended beneficiaries. The Secretariat had consistently raised with the authorities the need for improved access to beneficiaries and had reported these restrictions in standard project reports and project plans. For instance:

- We examined correspondence between WFP's Executive Director and Government officials between 1997 and 2004, expressing concern at the lack of unrestricted access to beneficiaries and seeking a list of beneficiary institutions to facilitate full and robust reporting of results. The provision of such lists had been recommended by our predecessors following their 1999 audit visit.
- The standard project report available to the EB members in 1997<sup>3</sup> noted that field visits required prior approval and were on occasion delayed or not completed.
- By 2005, WFP had achieved some improved access within DPRK and random access to participants in food for work. However, the 2005 report still noted difficulty in measuring progress against performance indicators due to Government restrictions on conducting surveys or monitoring.
- In September 2005 Governmental authorities required the number of monitoring visits to be reduced, in part as a result of reduced funding. WFP reduced the number of international monitoring staff from 20 to 15, assisted by 15 national staff.
- The project document approved by the EB<sup>4</sup> in February 2006 explained that the Government had indicated that monitoring would be significantly reduced, mainly in terms of the frequency of visits allowed, which would in future be quarterly. WFP planned to improve its operating conditions when implementing PRRO 10488.0, and to verify appropriate use of its assistance.

49. Our consideration of operating conditions since the implementation of PRRO 10488.0 in June 2006, showed that WFP had conducted 468 monitoring visits at an average of 58 per month. Under Article V of the Letter of Understanding between DPRK and WFP, the Government had agreed that WFP staff may travel wherever WFP food is distributed. The WFP DPRK Office has obtained agreement with the authorities to reduce the advance notice required for monitoring visits from one month to two weeks. Nonetheless we found that in 2007 the Country Office remained limited to one trip to each county every quarter, and three visits during the life cycle of each programme for programme assessment purposes.

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<sup>3</sup> 1996 report on project 5710.0 and 2005 project report 10141.3

<sup>4</sup> WFP/EB.1/2006/8/3



**Recommendation 5:** *We recommend that WFP should critically review the reliability of food monitoring statistics and continue efforts to extend field monitoring agreements to support unrestricted access wherever possible, to include translators supplied by WFP.*

## DIRECT PAYMENTS FOR PROJECTS UNDERTAKEN BY NATIONAL AUTHORITIES

50. DPRK's Ministries of Food Administration and Commerce are the main implementing partners responsible for food delivery to beneficiaries throughout the public distribution system in DPRK. The Ministry takes possession of WFP purchased commodities on arrival by shipping or railway and is responsible for internal transportation, storage and handling.

51. WFP reimburses part of the transportation costs at a fixed rate of US\$8 per metric tonne as a fuel subsidy: 50 per cent of which is payable as soon as the shipment is unloaded and 50 per cent on delivery in accordance with a pre-agreed distribution plan. We were unable to confirm the original calculation of US\$8 per metric tonne which had remained the same value since prior to 1997. Our review of project expenditure between 2001 and 2006 shows that fuel subsidy represented the main payment to Government counterparts, amounting to approximately US\$20 million.

52. The key management control over delivery and payment is the receipt of consignment notes which accompany delivery of commodities to the country level. This control allows WFP to collect information on food arrivals at entry points and to report on deliveries at the country level. In 2004, WFP's Oversight Services Division had reported that the consignment notes recorded delivery up to the warehouse from which food would be delivered to beneficiaries, and that consignee and consignor signatures sometimes belonged to the same person at the warehouse.

53. To provide assurance that food transportation met agreed objectives, we examined the project Letter of Understanding agreed in May 2006 between the Government and WFP. Article II confirms that no payment will be made for fuel costs where WFP has not been granted access or where consignment notes to the country warehouses have not been completed correctly. Annex 2 strengthens the payment conditions to ensure that fuel subsidy would not be paid for transportation to areas to which WFP is subsequently denied access.

54. Government officials are responsible for recording losses in the consignment notes. However, regular monitoring visits conducted by WFP indicated that government counterparts had not been recording food losses. To address this control weakness, the Country Office conducted training for counterpart staff in 2005-2006 on the proper recording and reporting of food losses. The Country Office continues to attempt to strengthen delivery oversight through training and discussion with the appropriate Ministries.

***Recommendation 6: We encourage the Secretariat to ensure robust reporting of post delivery losses and the maintenance of reasonable assurance over consignment delivery.***

## UNITED NATIONS BOARD OF AUDITORS' REPORT

55. We considered the audit report of the United Nations Board of Auditors issued by the Premier Président de la Cour des Comptes of France, the Auditor-General of the Republic of South Africa and the Chairman of the Philippine Commission on Audit. The report covered operations in DPRK from 2002 to 2006 by the United Nations Development Programme, the United Nations Population Fund, the United Nations Office for Project Services, and the United Nations Children's Fund.

56. The Board focused on management controls over staff hiring, foreign currency transactions, and monitoring access to projects; completing its review by gathering and examining support documentation, reports, and background papers; interviewing personnel; and verifying the evidence of findings previously raised by internal audit departments.

57. The Board reported that not all the UN organisations had complied with the relevant entities' instructions and procedures in relation to local staff hiring through DPRK government agencies, and local payments in foreign currencies. All local staff were seconded from the Government of DPRK and selected, nominated and appointed by the Government; and paid via the Government. UNDP had made some payments to local suppliers and local staff in foreign currency, contrary to the Standard Basic Agreement with the Government dated 8 November 1979 and relevant instructions; and the Board noted that the regulations and rules were not sufficiently comprehensive. The Board also confirmed that although project monitoring visits had taken place, these had been under the supervision of the DPRK authorities in all but one case examined.

58. The Board of Auditors concluded that it had addressed the focus areas that ACABQ had requested it to examine and provided findings and conclusions; and accordingly it did not suggest any further audit procedures to perform.

JOHN BOURN  
Comptroller and Auditor General, United Kingdom  
EXTERNAL AUDITOR

27 July 2007

**ANNEX 1**

**EXECUTIVE BOARD  
FIRST REGULAR SESSION  
ROME, 19-21 FEBRUARY 2007  
RESOURCE, FINANCIAL AND BUDGETARY MATTERS**

**Agenda item 6**

**WFP/EB.1/2007/6-E**

**EXTERNAL AUDIT OF FUNDS AND PROGRAMMES INVOLVED IN THE DEMOCRATIC PEOPLE'S REPUBLIC OF KOREA**

**WFP/EB.1/2007/6-E**

**INTRODUCTION**

1. In response to questions raised regarding United Nations operations in the Democratic People's Republic of Korea (DPRK), the Secretary-General proposed that an external audit of the Funds and Programmes involved in DPRK should be carried out. This paper outlines the implication of the Secretary-General's proposal for the World Food Programme (WFP).

**BACKGROUND**

2. WFP has conducted food assistance operations in the DPRK since 1995. A new PRRO 10488.0 for two years (2006-2007) was approved by the WFP Executive Board at its First Regular Session, 2006 (2006/EB.1/16) and began in June 2006 following the signing of a Letter of Understanding (LOU) by WFP and DPRK on 10 May 2006. The Executive Board was briefed on the status of the operations at its sessions in June and November 2006. WFP's DPRK operations have been audited by its External Auditor in 1999 and in 2005.

**SECRETARY-GENERAL'S PROPOSAL**

3. Opting to use the existing procedures within the United Nations System, the Secretary-General requested the Advisory Committee on Administrative and Budgetary Questions (ACABQ) under its authority in Article VII of the United Nations Financial Regulations and Rules, to request the United Nations Board of Auditors, to perform specific examination of the operations of any and all United Nations organizations, including the United Nations Funds and Programmes, which fall within the mandate of the Board of Auditors. The scope of the work should focus on past and current compliance with the applicable Financial Regulations and Rules, accountability frameworks and other directives as well as to ensure that money expended in DPRK went to the intended recipients. The areas to be reviewed should include foreign currency transactions, staff hiring, access to reviewing local projects and their outputs, and direct payments for National Execution (NEX) projects. The proposed period of review would be from 1998 to the present. It is also proposed that the Board of Auditors' review to be conducted within a time frame of 90 days.
4. The ACABQ, after considering the Secretary-General's proposal, has requested the United Nations Board of Auditors to carry out a special audit of the operations of United Nations organizations in the DPRK, including the United Nations Funds and Programmes which fall within the Board's mandate, as a matter of priority, and report its findings to the Advisory Committee. Recognizing United Nations Development Programme (UNDP) as the lead agency in the DPRK, the ACABQ has suggested that the United Nations Board of Auditors may also wish to consult the auditors of other United Nations entities.

## **WFP'S FINANCIAL REGULATIONS**

5. WFP does not fall within the mandate of the United Nations Board of Auditors. Sir John Bourne, the Controller and Auditor General of the United Kingdom, is currently the WFP External Auditor, Financial Regulation 14.5 stipulates that 'the External Auditor shall be completely independent and solely responsible for the conduct of the audit'. Furthermore, Financial Regulation 14.6 states that 'the Board may request the External Auditor to perform specific examinations and issue separate reports thereon.

## **CONCLUSION**

6. WFP is one of the main United Nations Funds and Programmes operating in the DPRK. The current request of the Secretary-General to the ACABQ does not envisage an audit of WFP operations given that the United Nations Board of Auditors does not have a mandate to audit WFP. However, in public statements the Secretary-General has emphasized a system wide assessment. WFP's External Auditor can undertake such an engagement either of his own volition by amending his workplan, or as a specific examination on the request of the Executive Board in terms of Financial Regulation 14.6.

## **2007/EB.1/8 External Audit of Funds and Programmes involved in the Democratic People's Republic of Korea**

Noting the Secretary General's proposal, the Executive Board decided to request the WFP External Auditor to carry out a special audit of the WFP operations in the Democratic People's Republic of Korea as a matter of priority and report its findings to the Board. The WFP External Auditor might wish to consult and coordinate with the United Nations Board of Auditors, which may be undertaking a special audit of United Nations organizations in the Democratic People's Republic of Korea, including the United Nations Funds and Programmes that fall within its mandate.

21 February 2007

**ANNEX 2**

Mr James Melanson  
President, World Food Programme Executive Board  
Embassy of Canada  
Via Zara 30  
00198 Rome  
ITALY

JBB/1255/07

29 March 2007

### World Food Programme Executive Board request for a special external audit of WFP operations in the Democratic People's Republic of Korea

I am writing to you in response to the Executive Board's request that the External Auditor carry out a special audit of WFP operations in the Democratic People's Republic of Korea as a matter of priority, and report findings to the Executive Board.

As Graham Miller advised you and the Executive Board during the Board's meeting on 21 February, we will be pleased to carry out a special audit as requested under Financial Regulations 14.6 and 14.5, as referred to in Executive Board paper WFP/EB.1/2007/6-E dated 19 February 2007 and the Executive Board's decision dated 21 February 2007. This will be a special audit in addition to the other work that we carry out under our programme of work for 2006-2007. We will coordinate our audit coverage with that being carried out by the UN Board of Auditors. We will report on the progress or outcome of this audit to the Executive Board at its meeting in June 2007.

**JOHN BOURN**  
**Comptroller and Auditor General, United Kingdom**  
**EXTERNAL AUDITOR**

## ANNEX 3

### Analysis of staff payments and value transfers made by WFP to the DPRK government and to local staff, January 2000 – April 2007

US\$	2000	2001	2002	2003	2004	2005	2006	Jan-Apr 2007	Total by Expense
<b>Local staffing cost paid to Government</b>	89,453	90,809	103,285	115,912	180,949	167,946	79,779	22,198	<b>850,331</b>
<b>Direct to local staff (US\$)</b>									
Lunch Allowance	31,846	32,517	43,521	44,212	45,617	43,258	36,849	11,633	<b>289,453</b>
Local Travel	325,928	234,967	342,683	258,495	307,727	252,536	42,884	15,990	<b>1,781,210</b>
International Travel	-	3,372	3,819	6,164	9,841	10,769	12,173	-	<b>46,139</b>
Driver's Salary	49,322	55,355	71,508	85,019	117,251	100,222	41,501	4,514	<b>524,692</b>
Driver's Overtime	2,998	4,677	4,723	2,724	3,355	4,376	3,279	709	<b>26,840</b>
<b>Total Staffing</b>	<b>499,547</b>	<b>421,697</b>	<b>569,539</b>	<b>512,526</b>	<b>664,740</b>	<b>579,107</b>	<b>216,465</b>	<b>55,045</b>	<b>3,518,665</b>
<b>Equipment transferred to Government</b>	7,827	12,120	-	-	436,237	24,269	-	-	480,453
<b>Total by Year</b>	<b>507,374</b>	<b>433,817</b>	<b>569,539</b>	<b>512,526</b>	<b>1,100,977</b>	<b>603,376</b>	<b>216,465</b>	<b>55,045</b>	<b>3,999,119</b>

1. Daily lunch allowances of €5 are paid to local staff. Originally payment had been in Euro, but since February 2007 payment are made in convertible DPRK won.
2. WFP pays an agreed local staff base salary currently €283 per month for semi-skilled, €293 for national officers and €311 for drivers to the Ministries providing the staff. WFP has no control over the amount paid to each staff member.
3. The value of equipment transferred to the Government is stated at the original cost of the equipment for use on a project, without taking into account the effect of depreciation at the time of transfer.