



**FOR INFORMATION**

FOURTH ITEM ON THE AGENDA

**Report of the Chief Internal Auditor a.i.  
for the year ended 31 December 2006**

**Report of the Chief Internal Auditor a.i.  
on significant findings resulting from  
internal audit and investigation  
assignments undertaken in 2006**

1. In accordance with the decision taken by the Governing Body at its 267th Session (November 1996), the Director-General transmits herewith the report of the Chief Internal Auditor a.i. on significant findings resulting from audit and investigation assignments carried out during 2006 (see appendix).
2. The Director-General considers the work performed by the Chief Internal Auditor to be extremely valuable in assessing strengths and weaknesses in operations, practices, procedures and controls within the Office. Recommendations made by the Office of Internal Audit and Oversight are thoroughly evaluated and there is constant dialogue between managers and the Chief Internal Auditor to give effect to them.

Geneva, 29 January 2007.

*Submitted for information.*

## Appendix

### Report of the Chief Internal Auditor a.i. on significant findings resulting from internal audit and investigation assignments undertaken in 2006

#### *Introduction*

1. The Office of Internal Audit and Oversight (IAO) of the ILO fulfils an independent oversight function established under article 30(d) of the Financial Regulations. Through audit, inspection and investigation processes, the IAO determines the adequacy and effectiveness of the Organization's system of internal control, financial management and use of assets. Its aim is to provide reasonable assurance that the activities have contributed to the attainment of the Organization's goals and objectives. More specifically, to achieve this, the IAO addresses the following audit objectives during its audit reviews: appraises accounting, administrative and operating controls; evaluates the responsible, efficient and economic use of the Organization's resources; ascertains the extent of compliance with established rules, regulations, policies, procedures and plans; determines the extent to which assets are accounted for and safeguarded from loss; assesses measures taken to prevent fraud, waste and malfeasance; ascertains the reliability of financial and management information; and examines the adequacy of the planning and monitoring system with regard to the operations, functions, programmes and activities within the Organization. Where necessary, the Chief Internal Auditor makes recommendations to improve their adequacy, efficiency and effectiveness. The IAO adopts a proactive approach to facilitating the assessment of risks and controls, and promotes a cohesive Office-wide approach to risk management and a learning culture in support of management's process to enhance efficiency, effectiveness and value for money in the activities of the Organization.
2. IOA does not develop or install procedures or engage in any activity that it would normally review or appraise or which could be construed as compromising either its independence or objectivity. The IAO has full and free access to all records, personnel, operations, functions and other material relevant to the subject matter under review. Its monitoring procedures are systematized to ensure that management properly follows up on, and implements, all audit recommendations. The results of the IAO's 2006 activities have not indicated any material weakness in the ILO's system of internal control in those areas audited. The IAO cannot, however, provide comment on those areas that have not been subject to an internal audit in 2006.
3. As regards the appointment of the Chief Internal Auditor, a separate paper will be presented to the Governing Body on this matter.

#### *Audit approach*

4. During 2006, the IAO modified its audit approach and reporting format to bring it more into line with generally accepted best practice within the internal audit profession. The IAO adopted the Committee of Sponsoring Organizations of the Treadway Commission (COSO) internal control framework as the basis for its audit approach. The COSO control framework was introduced in 1992 and is an internationally recognized control framework. When conducting assurance audits, the IAO will evaluate and report against the following criteria:

- **The control environment** – The control environment sets the tone of the organization or section being evaluated. Principal matters evaluated include management’s philosophy and operating style, integrity and ethical values, the organizational structure, the importance of the Executive Management and Governing Body, and commitment to financial reporting competencies. The control environment forms the basis on which the other aspects of the control framework (discussed below) rest.
  - **Risk assessment** – The identification and analysis of relevant risks to achieving the Organization’s objectives forms the basis for determining control activities.
  - **Control activities** – Control activities occur throughout the Organization and address risks. The range of activities includes the assignment of responsibilities, division of duties, adequate audit trails, and preventative, detective and corrective controls.
  - **Information and communication** – Information and communication must effectively flow throughout the Organization in all directions. The objective is to capture pertinent information in a form and within a time frame which allows people to carry out their responsibilities. Information systems and communication processes should embody sound management practices, and facilitate control activities.
  - **Monitoring** – Effective monitoring is proactive and comprises ongoing monitoring of activities by both staff and management, the evaluation of compliance with internal controls, as well as timely reporting and taking of actions to address risks, or to prevent the occurrence of undesirable situations.
5. The aim of adopting this new approach is to bring a more integrated and strategic approach to the IAO’s assurance audits to facilitate the identification and reporting to management of significant issues in a timely manner.

### ***Audit at headquarters***

#### Internal Administration Bureau (INTER)

6. The objectives of this audit were to assess the accuracy and completeness of financial and management information; efficiency, effectiveness and economy of operations; compliance with rules, regulations, policies and procedures; the degree to which assets are safeguarded from loss. The audit also included a review of the Communication and Files Section (DOSCOM) and the ILO’s Security Unit (SECURIT), which form part of INTER.
7. The IAO noted cases where both management and staff have made efforts to comply with rules and regulations. However, various matters of importance were addressed in the report, and the IAO has made recommendations which in its view address core issues, and not merely the symptoms of various weaknesses identified in the control environment as a whole.
8. The IAO identified an opportunity to improve both accounting and operating controls to further reduce the risk of non-compliance with rules and regulations. The IAO also identified scope to improve INTER’s system of maintenance and operational planning. Similarly in the area of the development of end-user applications, the IAO recommended improvements in the system of internal control. More specifically in this regard, the IAO recommended expanded involvement of INTER staff and staff from other units in the development process; and that, to help ensure future system development activities comply with best practice, the accepted norms of the Systems Development Life Cycle be followed.

9. The level of documentation held on file to ensure that a proper audit trail is maintained was found in some cases to be inadequate and, therefore, required improvement. In order to ensure completeness of record keeping and enhance transparency, the IAO recommended that INTER determine the level of documentation required to maintain an appropriate audit trail for each transaction.
10. Regarding procurement, the IAO noted that in certain areas where compliance with rules and regulations is required, specifically in the case of large contractual commitments relating to IT systems maintenance, evidenced and correct contracting procedures had been followed. On occasion, however, the IAO noted established financial and administrative work processes had not been strictly adhered to. The IAO, therefore, recommended that the Office take steps to ensure that established work processes are duly followed by involving PROCUREMENT in all aspects of the procurement process above decentralized levels, as was recommended in an earlier the IAO report on procurement. The IAO further recommended that the role of the Financial Certifying Officer within INTER be reinforced.

#### Communications and Files Section (DOSCOM)

11. DOSCOM was found to be well managed and administrative work was assessed as good. Substantial cash flow savings and efficiency gains in the Office's postal expenses have been realized over the past two biennia, which is commendable. There is, however, scope for improvement in the documentation of rules and regulations relating to communications and records in the ILO.
12. Currently, only certain incoming correspondence is manually recorded, and alternative methods of recording incoming correspondence, as proposed by the IAO, will not adequately address the issue. The introduction of the Electronic Document Management System should, however, solve the issue.
13. The Archives Committee which had not convened since 1998 has now been reconstituted (as recommended by the IAO in the audit report), and held its 33rd Session in September 2006. The Committee is in the process of addressing various audit recommendations relating to revising communication and records circulars, and clarifying matters relating to filing plans, especially with field offices.
14. The IAO noted that a large backlog existed in terms of files to be archived, some dating back to at least 1971. As the archives are the only complete historical record of the Office's activities since its inception, the IAO recommended that, funds permitting, serious consideration should be given to the employment (on a short-term basis if necessary) of a qualified archivist to assist in the task of reducing the backlog.
15. In response to the IAO's recommendation that a risk-based management approach be adopted in the DOSCOM environment, a risk-assessment and evaluation project has been started by INTER, and addresses risks and opportunities faced by DOSCOM as identified in the audit report, as well as other matters.

#### ILO Security Unit (SECURIT)

16. The operations management of SECURIT was found to be satisfactory, although a more formalized approach to managing the section, together with enhanced review of operations, was identified as an opportunity for improvement. The IAO has suggested that a risk-based approach to managing the section would be appropriate.
17. It was noted that job descriptions for the security guard positions were not prepared in the past, although draft job descriptions were in the process of being prepared and discussed

with security staff at the time of audit. The IAO also noted that procedures to be followed by the SECURIT in an emergency had not been formally documented. The IAO, therefore, recommended that both formal job descriptions and emergency procedures be finalized and documented.

### ***Audit of field offices***

18. During 2006, the IAO visited one Regional Office, which included a subregional office and one external office in the Africa Region. The audit's objectives were to evaluate the efficiency and effectiveness of operations, including the adequacy of the internal planning and monitoring system with regard to the operational activities of the Office; the extent of compliance with established policies, regulations and rules; the reliability of financial information for management and reporting purposes; and the extent to which assets were accounted and safeguarded from loss.
19. The audit field work for the abovementioned offices has been completed. The IAO is in the process of reporting, and will present any significant findings in its next report.

### ***Audit of technical cooperation projects***

20. The IAO conducted audits of two technical cooperation projects: the International HIV/AIDS Workplace Education Programme in Ethiopia, which has a budget of US\$949,432 that funds activities over a three-year period, May 2004 to April 2007; and Supporting the National Plan of Action for the Elimination of the Worst Forms of Child Labour in Kenya, which has a budget of US\$5 million that funds activities over a four-year period, September 2004 to September 2008. Both projects are funded by the US Department of Labor.
21. The audit field work for each project has been completed and the IAO is in the process of reporting. The significant findings arising from each audit will be presented by the IAO to the Governing Body in its next report.

### ***International Training Centre of the ILO (ITC)***

22. The IAO conducted an audit of external collaborator contracts issued by the ITC, covering the period 2004–05, and reported its findings to the ITC management in 2006. In the IAO's view, the ITC's policies and guidelines concerning external collaborators, which underwent extensive revisions, are adequate to promote transparency and accountability when selecting and hiring external collaborators. The IAO made further recommendations to enhance control over the use of external collaborators; bring efficiencies to the administrative process; and aspects of financial control.
23. The IAO is pleased to note the ITC's management has reported that it has implemented the majority of the IAO's recommendations and is actively addressing those that have not yet been implemented. The IAO shall prepare a summary of its report which will be submitted to the next ITC Board Meeting by the Director of the Centre.

### ***Joint Staff Health Insurance Fund of the ILO and ITU (SHIF)***

24. The control environment of the SHIF was evaluated as good; however certain significant matters requiring attention were reported.

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## Fund Liquidity – Fund contributions received and benefits paid

25. The Fund has for the past three years experienced a situation in which actual contributions received from members have fallen short of benefits paid. Were this situation to continue, the future financial viability of the Fund would be threatened. In order to return the Fund to the required level of liquidity, various scenarios relating to differentiated contribution rates were prepared by the Executive Secretary and were presented to the Fund's Management Committee. Simultaneously, an in-house actuary was engaged to prepare future actuarial valuations and predictions under the various scenarios presented. The Executive Secretary has assisted the members of the Fund's Management Committee in assimilating financial and operational concepts, principles of prudential management and financial norms and measurements applicable to health insurance.
26. The Management Committee is evaluating proposals which will include measures for implementation in 2008, to restore the fund's medium term viability, but no decisions have as yet been taken. The IAO therefore recommends that the Management Committee of the Fund should take the necessary decisions regarding the future of the fund as soon as possible, taking into account the fact that the future of the fund is dependent on its financial viability.

## Continued and uninterrupted operation of the Health Insurance Information System (HIIS)

27. The SHIF IT/IS staff member responsible for the operation and maintenance of the system is the only staff member to have the necessary knowledge of the system to maintain its day-to-day functionality. Should the staff member become incapacitated for any length of time, there is a risk that the system would effectively cease to function.
28. It was recommended that another staff member of the Office, not involved in the manual checking of input, processing or output of the HIIS, be trained in the basic batch payment functionalities of the HIIS. This would ensure that, in the absence of the SHIF IT/IS staff member, payments can still be made to claimants. The Executive Secretary should identify a suitable person, possibly from a department or section other than SHIF.

## **Investigations**

29. The IAO is in the process of conducting two investigations into allegations of financial irregularities. As both investigations are ongoing, and to respect due process, The IAO shall present its findings in its next report.

## **Assistance to the Selection Panel to appoint the External Auditors of the ILO**

30. In 2006, one of the major activities undertaken by the IAO was to provide secretariat and technical support to the Selection Panel appointed by the Governing Body to make recommendations on the appointment of a new External Auditor. The IAO assisted the Panel with its task of evaluating applications received. The Office proposed that the IAO provide such support to the Panel as the IAO is independent of line management, and has the necessary technical skills to evaluate proposals received in an objective and independent manner. The Panel describes its work in GB.298/PFA/2.

## **Audit Needs Assessment and Strategic Plan**

31. During 2006, the IAO prepared and completed an Audit Needs Assessment and Strategic Plan, which was submitted to the Director-General in early December 2006. The IAO's

Audit Needs Assessment and Strategic Plan provides an outline of the long-term planning proposal of the work of the IAO. Its aim is to determine the level of audit coverage required to provide the necessary assurance to the Director-General and the Governing Body on the ILO's system of internal control; and also provides an estimate of audit resources and skills (e.g. specialist IT audit and investigation skills) required to meet the long-term audit programme. It provides the Office with the opportunity to assess if the current level of audit resources is sufficient to meet the programme of audit work proposed in the strategic plan.

32. The Audit Needs Assessment and Strategic Plan is driven by a philosophy of adding value to assist the ILO to improve the operations, controls and structures, programmes, and processes that contribute towards achieving its objectives. A key element of the Audit Needs Assessment is, therefore, to help ensure that internal audit resources are properly directed to risk areas. As the ILO does not have in place a formal and structured system of risk management on which the IAO could place reliance, the IAO undertook its own risk-assessment exercise, which involved consultation with ILO management. IAO's analysis identified 110 auditable areas, which were then ranked according to the results of the risk assessment. This analysis, combined with the audit approach set out in the Audit Needs Assessment, was used to inform the IAO's audit priorities for this and the next two biennia.

### ***Risk management***

33. As mentioned above, the Audit Needs Assessment and Strategic Plan noted the lack of a formal system of risk management within the ILO. Risk management complements the application of a results-based management framework in that it helps management to focus their efforts on the achievement of objectives by assessing actions necessary to mitigate events that may hinder achievement of those objectives, or identify opportunities to facilitate the achievement of objectives. The IAO has begun to raise awareness of risk management within the ILO by referring to this subject in its internal audit reports.
34. The Chief Internal Auditor a.i. participates in the IRIS Field Roll-Out Task Team in the capacity of an observer. Risk management is conducted as part of the field roll-out processes, consisting of regular assessments by the Task Team of those events which could impair the achievement of a smooth and successful IRIS field roll-out, and action needed thereon to mitigate those risks.
35. Implementing an Office-wide system of risk management is the responsibility of management and should be provided for as a milestone to be achieved in 2008 in the Results-Based Management Roadmap.

### ***External quality review and internal audit charter***

36. In 2003 the IAO adopted the Professional Standards of the Institute of Internal Auditors (IIA) – GB.289/PFA/7 refers. The IIA standards require that internal audit departments undergo an external quality review at least once every five years to ensure the adequacy and effectiveness of internal audit functions. During 2007, the IAO intends to commission an independent external quality assurance review, which will be undertaken by an accredited assessor. This will be the first time the IAO will undergo such a review.
37. The aim of the review will be to assess the overall quality of the IAO's audit programme and the extent to which the IAO is in compliance with the IIA standards. Only if the IAO has demonstrated that it has complied with the IIA standards to the satisfaction of the external assessor can the IAO report that it has "conducted its audits in accordance with the Standards for the Professional Practice of Internal Auditing".

38. The IIA standards also require that internal audit departments have in place an Internal Audit Charter approved by the “board” or in the case of the ILO, the equivalent being the Governing Body. A charter is a formal written document that defines the internal audit department’s purpose, authority, responsibility and scope of internal audit activities. An internal ILO circular was issued in March 2002 that covers much of the requirements of an Internal Audit Charter. The IAO shall use this as a basis to prepare an audit charter and submit it to the March 2008 Governing Body requesting approval. This is an important step in complying with the IIA standards as it further underpins the authority, purpose and remit of IAO activities.

### ***Follow-up on internal audit recommendations***

39. The responses to implementation of the IAO’s recommendations by headquarters units and field offices have on the whole been good. There are some instances, however, where full reporting on audit recommendations remains to be completed. In one case, a field office has not responded at all to the IAO’s request for an implementation report and, in another, it took a field office over one year to address two straightforward yet important recommendations. The IAO is actively following up on all outstanding cases.
40. The IAO continues to provide guidance and assistance to management, as considered necessary, to give effect to all recommendations.