

# **Statement on Internal Control**

## **Scope of Responsibility**

As the Director of the Pan American Health Organization (PAHO), I have responsibility for maintaining a sound system of internal control that supports the achievement of PAHO's mandate and objectives, while safeguarding the funds and assets administered by PAHO, for which I am responsible, in accordance with the responsibilities entrusted to me in the PAHO Constitution, by the Governing Bodies, and in the Financial Regulations of the Organization.

Accountability is an integral component of PAHO's Results Based Management (RBM) framework and, as such, empowers managers to take the necessary steps to achieve their expected results, while requiring the exercise of due diligence in actions and decisions, and compliance with applicable regulations and rules. Delegation of Authority is a prerequisite for the successful implementation of RBM. Good governance is enabled by the appropriate delegation of authority and, as Director, I have approved a Delegation of Authority framework that delineates clear lines of authority over all available resources, both human and financial, and includes the responsibility and accountability of personnel across the Organization.

Accountability at PAHO carries with it the obligation to report on the discharge of one's delegated responsibilities through established mechanisms, including the annual certification of financial information and the assessment of the status of the implementation of the biennial work plan.

## **The Purpose of the System of Internal Control**

The system of internal control is designed to manage risk to a reasonable level rather than to eliminate all risk of failure to achieve expected results and strategic objectives. It can therefore only provide reasonable and not absolute assurance of effectiveness. The system of internal control is based on an ongoing process designed to identify and prioritize the risks to the achievement of the Organization's mandate and objectives, to evaluate the likelihood of those risks being realized and the impact should they be realized, and to manage them efficiently, effectively, and economically. The system of internal control has been in place at PAHO for the financial reporting period 1 January 2015 through 31 December 2015, and up to the date of the approval of the Financial Report of the Director.

The foundation for the system of internal control at PAHO lies in the Constitution of the Pan American Health Organization and the Financial Regulations. From this, the Organization has developed and employed additional tools to further inform and guide the control framework, such as the Country Cooperation Strategy (CCS), Staff Rules and Staff Regulations, the E-Manual, the Standard Operating Procedures (SOP) and the Job Aids (JA), Personnel Performance and Evaluation System (PPES), Performance Monitoring and Assessment (PMA), and the Financial Accountability Framework.

## **Capacity to Handle Risk**

As the Director of PAHO, I have taken note that a system has been created of core and cross-functional teams which have overall responsibility for identifying and assessing risks associated with the implementation of the Program of Work and the overall operations of the Organization. Core teams include the Ethics Office, the Office of Legal Counsel, the Country Focus Support Office, the Department of Planning and Budget, the Department of External Relations, Partnerships and Resource Mobilization, the Department of Human Resources Management, and the Department of Financial Resources Management. These core teams are responsible for establishing the control environment, and providing the discipline and structure for the achievement of the primary objectives of the system of internal control.

Some examples of key cross-functional teams include the Integrity and Conflict Management System (ICMS), the Asset Protection and Loss Prevention Committee (APLPC), the Property Survey Committee, the PAHO Infrastructure Investment Projects Committee (PIIC), the Investment Committee, the Disaster Task Force, and the Epidemic Alert and Response Task Force.

Furthermore, the Office of Internal Oversight and Evaluation Services serve as an advisor to the Director, as well as an advisor and observer on these cross-functional teams.

## Risk and Control Framework

The risk and control framework is developed and implemented by the Governing Bodies and the Pan American Sanitary Bureau (PASB), the Secretariat of the Organization. These organs, as stipulated in Article 3 of the Constitution of PAHO, determine the Organization's general policies, including financial policy, and review and approve the multi-year strategy and biennial program and budget of the Organization.

The Secretariat provides regular reporting to the Governing Bodies on the financial, program and budgetary status of the Organization, including an annual report by the External Auditors of PAHO. Furthermore, the Office of Internal Oversight and Evaluation Services (IES) issues an annual report of its activities, with a status of outstanding audit recommendations. The Auditor General also provides the Director with an overall opinion on PAHO's internal control environment. For the financial reporting period 1 January 2015 through 31 December 2015, the Auditor General has concluded the following (draft):

*Based on the findings of its internal audits and its other internal oversight activities in 2015 (and in previous years), and taking into account the findings of other sources of assurance, IES's overall opinion is that PASB's internal control environment continues to provide reasonable assurance for the safeguarding of assets; the accuracy and timely recording of transactions; and the mitigation of risks to the achievement of the Organization's objectives.*

*A large-scale information systems development like the PMIS modernization project entails implementation risks, but it also offers a major opportunity to enhance the efficiency and effectiveness of the PASB's internal control environment. At the time of this writing, it is too early to assess the impact of PMIS on internal controls. However, the PMIS is expected to result in a significant improvement in internal controls by embedding controls into automated processes and by improving information flows, thereby reducing risks in the execution of administrative and financial transactions.*

*Under the "three lines of defense" concept of institutional governance theory, management is responsible for the system of internal control. The first line of defense is provided by the day-to-day, risk mitigating operations and internal controls that management has set in place. The second line comprises managerial review activities, including Enterprise Risk Management and the monitoring of compliance with regulations, rules and policies. The third line of defense, which operates behind management's first and second lines, is the assurance provided by internal auditors (and others). The PMIS should provide better information and clearer audit trails, thereby ameliorating all three lines of defense.*

*Absolute assurance on the internal control environment is, of course, impossible, owing to inherent limitations for most internal controls. Some internal controls may be rendered temporarily inadequate, owing to factors like error, intentional over-riding, and evolutions in the risks that the internal controls address. A current inhibiting factor on the improvement of internal controls at the country office level is the outdated Manual for Country Office Operations, whose most recent revision took place in 2007. In the near-decade since the Manual was last reviewed, the evolution of administrative practices, the introduction of International Public Sector Accounting Standards and the PMIS project have all introduced new working practices. IES's internal audits have found inconsistencies in administrative practices at the country office level, as individual country offices have introduced local practices in the absence of clear guidance from PASB Headquarters. PASB management has indicated to IES that it is considering a replacement of the outdated Manual by new Standard Operating Procedures. This initiative will be a significant step in encouraging a greater consistency in Organization-wide administrative practices.*

*To further strengthen the PASB's internal control environment, the linking of risks to Organizational objectives and to risk-mitigating internal controls needs to be clearer. Management is currently working on a more clearly-defined Internal Control Framework and, in parallel, a more focused Enterprise Risk Management process that prioritizes key risks and their mitigating measures. In this way, the connections between the Organization's objectives, risks, and risk-mitigating internal controls are becoming gradually clearer.*

The Departments of Financial Resources Management (FRM) and Planning and Budget (PBU) submit monthly reports to Executive Management covering the Organization's current financial position, the likelihood that financial and budgetary plans will be achieved, and the risks attached. These reports are discussed in detail in order that the members of Executive Management have appropriate and comprehensive information necessary to the decision-making process. In addition, a corporate Performance

Management Assessment process (PMA) is conducted semi-annually, which involves Executive Management, Entity Managers, and technical staff to assess progress towards the program of work and the Strategic Plan.

A fully functional Enterprise Risk Management (ERM) system is critical to control the pace and manner of change in the Organization resulting from the adoption of new technology, the expansion of technical cooperation requirements of Member States, the growth in resources under administration, and adapting to UN transformation. In 2011, PAHO's Executive Management team approved the conceptual framework of the ERM.

The objectives of PAHO's risk management approach are twofold: to support informed decision-making and to embed risk management in corporate operational processes. In this regard, the ERM program has two lines of work; one related to the risk register (RR) and the other related to corporate risk. The RR was created with the purpose of integrating the identification of risks and opportunities as part of the managerial thinking for planning, implementation and the monitoring of the biennial work plans (BWP) at the entity level. By definition, the risk register has a time horizon of two years and should be considered as a tool that supports management processes and to identify systemic issues. Corporate risks are managed by the top level of PAHO's Secretariat (Executive Management) and focus on those risks that might affect the capacity of the Organization to perform and comply with its mission and mandate. The time horizon for these risks is between three and five years.

To this end, the Enterprise Risk Management (ERM) program is implementing a corporate risk management policy that establishes tools to identify, assess, respond to and monitor risks in a structured, systemic and prompt manner. In compliance with the ERM Policy, risk assessments were included as part of the 2014-2015 biennial operational planning process, and the Risk Assessment Methodology was included in the Operational Planning Manual 2014-2015. All PAHO entities were required to identify the risks and mitigation actions when were necessary for the biennial work plan 2014-2015. In December 2014, a new Risk Register tool and guidelines were released, with guidelines. The RR is reviewed by the ERM advisor on a regular basis to help prioritize management action, monitor mitigation actions and facilitate accountability towards EXM.

At the corporate level, the ERM Standing committee was reestablished in September 2015. The Committee membership includes senior level officials selected from each Executive Management Office, as well as CSC, with IES as an observer. The Enterprise Risk Management Advisor acts as the technical secretariat of the Standing Committee. A process was defined to identify the corporate risks, and from there to assess, validate and prioritize the risks. A risk heat map was developed and agreed at the senior level.

### **Review of Effectiveness**

As the Director of the Pan American Health Organization, I have responsibility for reviewing the effectiveness of the system of internal control. My review of the effectiveness of the system of internal control is informed by the work of the Office of Internal Oversight and Evaluation Services (IES), by the senior managers within the Organization who have responsibility for the development and maintenance of the internal control framework, and by the comments made by the External Auditors in their management letters and audit reports. I have been advised on the implications of the result of my review of the effectiveness of the system of internal control by the Auditor General and the Audit Committee. A plan to address identified weaknesses and ensure continuous improvement of the system is in place.

The Auditor General reports directly to me. IES undertakes independent and objective assurance and advisory activities, which are designed to improve and add value to the Organization's operations. Using a systematic, risk-based approach, IES seeks to assist the Organization to achieve its objectives by auditing the effectiveness and efficiency of organizational governance, internal controls, operations, and processes. IES undertakes internal audit assignments, for which very precise objectives are established through an assessment of the relevant risks. On the conclusion of an oversight assignment, IES prepares a detailed report addressed to me, and copied to concerned individuals in the Secretariat. The assignment reports include findings and recommendations to help management address risks, maintain or enhance internal controls, and encourage effective governance. IES systematically follows up on all the recommendations it makes. In addition, IES provides support to evaluation activities throughout the Organization, recording and monitoring all evaluation assignments undertaken across the Organization.

The PAHO Audit Committee, which was established pursuant to Resolution CD49.R2, serves in an independent expert advisory capacity to assist the Director and PAHO's Member States. It provides independent assessment and advice on the operation of the Organization's financial control and reporting structures, risk management processes, and the adequacy of the Organization's systems of internal and external controls. The Audit Committee meets twice each year, and met in April and November of 2015.

The system of internal control has been in place for the year ending 31 December 2015 and up to the date of the approval of the Financial Report of the Director. However, with the significant growth in the Organization, a number of weaknesses in the system of internal control were identified that have necessitated additional work to be undertaken in order that adequate internal control assurances could be provided.

| Significant Internal Control Issues  | Actions Taken to Address Issues  |
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| <p><b>1. Corporate Administrative Systems -</b><br/>                     The implementation of International Public Sector Accounting Standards (IPSAS) highlighted the weaknesses of legacy systems,</p> <p>The implementation of the PMIS, an Enterprise Resource Planning (ERP) system, integrated Program Planning, Budget, Finance and Human Resource administration, providing more accurate and comprehensive real-time information. It also requires an increased level of interaction with the ERP by all staff, providing accurate data and extracting necessary information in a decentralized environment. Extensive training for all staff in PMIS business processes was launched in 2015 and will need to continue in 2016.</p> | <p>Workday was implemented as the core ERP for PAHO covering Human Resources, Payroll (January 2015), Procurement and Finance (January 2016). Tidemark provides reporting against planned amounts; In-tend covers Tendering; and, G-Treasury provides the Treasury functionality not covered by Workday.</p> <p>A training plan was implemented based on the competency needs and gaps as identified during the design and test phases of the Implementation Plan for the system. The training plan will be continuously updated and enhanced as needs are identified.</p> <p>While the PMIS implementation will continue to require close monitoring, it has addressed the legacy internal control issues.</p>  |
| <p><b>2. Project Implementation -</b><br/>                     Effective implementation of the Program and Budget is critical to the reputation and sustained growth of the Organization. The balance of Voluntary Contributions commitments that remain unimplemented, as well as the funds returned to donors, has continued to be a concern. A balance of project acceptance and design, rational business practices, policies and procedures, and absorptive capacity of beneficiaries is required to reach optimal project implementation goals.</p>  | <p>Over the years, the PAHO Secretariat noted an increasing need to address a range of gaps in supporting project management, including the negotiation, development, monitoring and impact evaluation of voluntary contribution grants. In July 2013, a special retreat was chaired by the Director of PAHO where project management and voluntary contributions policies and procedures within the Pan American Sanitary Bureau were discussed in-depth.</p> <p>In March 2014, a Resource Management Framework (RMF) was approved by the Director. As part of the process of implementation of the RMF, in May 2014, a working group was established to review current business processes associated with the implementation of grants, and to identify immediate actions to improve project management in the Organization. Among the recommendations from the working group was the need to “update the policy and workflow for the corporate review of voluntary contributions in PAHO”.</p> <p>In June 2015, the DD and AD appointed the Project Cycle Working Group to work on reviewing the current process and identifying gaps and opportunities for improvement. The working group was composed by the following entities: ERP as Chair, AD’s office as co-chair, DD Office, PBU, CSC, CHA, FRM, PWR-ECU, and LEG.</p> <p>The group worked on two sets of recommendations. General recommendations aimed at addressing issues over the whole project cycle and specific ones focused on simplifying the Project Review Process.</p> <p>The Project Cycle Working Group issued a report with</p> |

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|   | <p>recommendations, which was presented and recommendations approved by EXM in December 2015.</p> <p>Since November 2015, the function of steering the Project Review Process was transferred from PBU to ERP, according to GIB HQ-FO-15-505. Since then, ERP has been working on the implementation of the recommendations including:</p> <ul style="list-style-type: none"> <li>• Develop portfolio of projects;</li> <li>• Establish an electronic tracking system;</li> <li>• Produce regular statistics and analysis;</li> <li>• Strengthen evaluation and lessons learned aspects on project implementation;</li> <li>• Improve information sharing on project implementation and evaluation results;</li> <li>• Continue to strengthen project management in the Organization;</li> <li>• Monthly executive summary reports;</li> <li>• Work with FRM to improve analysis of information shared through Project Implementation Review (PIR) Report;</li> <li>• Engage the Program Management Network;</li> <li>• Support PBU on monitoring the implementation of projects;</li> <li>• Keep fluid and continuous contact with technical departments.</li> </ul> <p>The Project Cycle Working Group also elaborated the work flow for the different group of initiatives with the purpose of simplify and expedite the review process. EXM approved the new workflows presented by ERP for project proposals, which are currently being introduced and implemented in the review process.</p> |
| <p><b>3. Succession Planning -</b><br/>                     The ongoing retirement of senior managers has the potential to result in a loss of institutional knowledge.</p> | <p>During the 2016-2017 BWP and HR plan review, the Director expressly addressed the need of succession planning with managers, and the following statements were indicated by the Director during the review: The Director and EXM will review all vacant posts (current and those that will become vacant in the new biennium) to ensure profiles are aligned with the PAHO Strategic Plan, PAHO's People Strategy, and corporate mandates.</p> <p>Extensions beyond retirement will not be considered. Managers need to carefully analyze opportunities for re-profiling and ensure that where retirement is approaching to move expeditiously with the recruitment process. In addition, the People Strategy also addresses this as reflected in theme 1 – Strengthening alignment and agility. It is expected that the implementation of the Strategy will begin during the 2016-2017 biennium.</p>   |

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| <p><b>4. Emergency Response</b><br/>                     PAHO, as the preeminent health agency in the Region of the Americas, must take a leadership role in addressing emergencies. The impact and severity of recent emergencies in the Region have highlighted the need to have a strong, decentralized team of specialists to analyze and coordinate response requirements and information.</p>  | <p>The implementation of PAHO’s institutional response to emergencies and disasters (IREDD) policy, approved in 2012, continues to strengthen and enhance the ability to respond to emergencies and disasters in the Region. In 2015, the Department of Emergency Preparedness and Disaster Relief (PED) provided technical support across the Region, including key action orientation to all new PAHO Representatives and workshops in Nicaragua on PAHO Emergency Response Procedures to Administrators of 18 Country Offices (CO) and Disaster focal points of 22 CO. Furthermore, PED was successful in mobilizing resources in response to Member States requests for support in emergency situations in 2015, including: support to internally displaced populations in Colombia, drought in Honduras,, cholera in Haiti, severe floods in Chile, St. Vincent and the Grenadines, St. Lucia, Dominica, and Paraguay, and earthquake in Guatemala. As established by the IREDD, PAHO activated the Incident Management System to support Member States readiness for Ebola and emergency response to Zika.</p>  |
| <p><b>5. International Economic Environment -</b></p> <ul style="list-style-type: none"> <li>• The prolonged challenging global economic environment, the dollar evolution, and the decline of raw material prices impact all Member States and present several risks to the Organization’s ability to fund the Budget: Member States have continued to espouse a policy of zero to minimal nominal growth to the Budget.</li> <li>• The low interest rate environment has reduced the investment income earned and available to supplement the Member States’ Assessed Contributions.</li> <li>• Exchange rates in some primary countries have fluctuated significantly during the year, resulting in additional uncertainties regarding the value of some transactions locally.</li> </ul> | <p>The Organization has a conservative Investment Policy overseen by the Investment Committee. The Investment Committee meets in person at least twice each year to review the performance of the investment portfolio and regularly invites experts to these meetings to discuss the various risks in the portfolio, as well as their forecast of the economic environment. The Investment Committee has contracted three external investment managers to manage approximately \$300 million of the \$600 million portfolio, thus taking advantage of expertise, economies of scale and opportunities in the market in order to maximize the yield on available resources while preserving the principal.</p> <p>The Organization monitors exchange rates in the country offices, and manages the local currency bank balances accordingly. Exchange rate gains and losses are allocated based on the source of the funds. However, as the Budget is denominated in US dollars, fluctuations in local exchange rates will still impact the country office’s “buying power” even if their revenue and expenses are denominated in local currency, although with smaller associated exchange risks. Country Offices work closely with the Department of Planning and Budget to address these issues.</p> |
| <p><b>6. Funding of Long-Term Employee Liabilities -</b><br/>                     With the implementation of IPSAS in 2010, the Organization recognized the assets and liabilities of the Organization, resulting in a more transparent picture of the true financial status of the Organization. The long-term liabilities associated with After-Service Health Insurance (ASHI) and Termination and Repatriation Entitlements Plan (TAREP) were recorded on the Statement of Financial Position in 2010, and irrevocable trusts were established for the financial resources available to fund these liabilities (plan assets). While several initiatives have been implemented to provide some funding on both an annual and ad hoc basis, the Organization does not have a</p>           | <p>Currently, PAHO is assessing a 4% surcharge on staff payroll to provide funding towards the ASHI liability. Revenue from this surcharge totaled \$3.1 million in 2015. An additional \$1.0 million of investment net income earned on the irrevocable trust assets was also credited to the Trust.</p> <p>In January 2016, \$8.0 million was transferred from the SHI reserve to the ASHI Trust Fund.</p> <p>PAHO and WHO are considering combining the liabilities and assets of the PAHO/WHO ASHI to achieve efficiencies in meeting funding objectives. It is expected that the funding</p>   |

PAN AMERICAN HEALTH ORGANIZATION  
 FINANCIAL REPORT OF THE DIRECTOR and REPORT OF THE EXTERNAL AUDITOR  
 1 January 2015 – 31 December 2015

| Significant Internal Control Issues  | Actions Taken to Address Issues   |
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| comprehensive plan to fully fund the ASHI liability over a determined period of time.  | strategy and other measures under consideration will enable PAHO to achieve full funding in the next 20-30 years depending on assumptions about the future evolution of health care costs and investment yields.  |
| <p><b>7. IT security of PAHO’s Headquarters Network</b><br/>                     The strength of the security controls in place to access the headquarters IT network presents risks to the integrity of the Organization’s proprietary information.</p> | <p>In 2015, information security controls were implemented to activate content, filtering, and monitoring capabilities. The old firewalls in HQ were also replaced with state of the art (Palo Alto) devices. These appliances block new threats and have significantly improved the security controls in place to access the headquarters IT network. This was the last recommendation pending from the assessment completed by two independent security companies.</p> <p>While the threats and information security controls will continue to require close monitoring and continuous enhancements, the issue regarding inadequate security controls has been addressed.</p> |

**Conclusion**

I am confident that as a result of the actions taken to address the significant issues noted above, the system of internal control will continue to be strengthened. Therefore, in my opinion, the Organization’s system of internal control was effective throughout the financial reporting period 1 January 2015 through 31 December 2015, and remains so on the date I sign this statement.

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**Carissa F. Etienne**

**Director**

**Pan American Health Organization**