

Report of the External Auditor

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TRIBUNAL DE CUENTAS
DE ESPAÑA

The Pan American Health Organization

Long Form Report on the 2013 Financial
Statements audit

The aim of the audit is to collaborate with the audited organization in order to reach its objectives, while supporting compliance with principles of transparency, legality and sound financial management.

The Spanish Court of Audit (SCA), headed by its President, provides external audit services to international organizations, working independently of its role as the Supreme Audit Institution of Spain. The President and the SCA are independent of the Spanish Government and ensure the proper and efficient spending of public funds and accountability to the Spanish Parliament. The SCA audits the accounts of all public sector bodies as well as political parties, collaborates in works related to its role as an active member of INTOSAI and EUROSAI and takes part in audit works within European Union projects and beyond.

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1. Executive Summary

1.1. Introduction

- 1 We have provided an unqualified audit opinion on the 2013 consolidated financial statements of the Panamerican Health Organization (hereinafter PAHO) which present fairly, in all material respects, the financial position and the results of operations and cash flows for the financial period ended 31 December 2013; and we confirm that this audit revealed no weaknesses or errors which we considered to be material to the accuracy, completeness and validity of the consolidated financial statements.
- 2 The 2013 consolidated financial statements of PAHO represent the fourth year in which the International Public Sector Accounting Standards (IPSAS) have been used. This unqualified opinion means that IPSAS are embedded within the Organization accounting management.
- 3 However, like the previous year, we noted that the computer system which supports accounting is outdated; it was not designed for an accounting system based on accrual criteria and requires manual adjustments at the end of the period. We encourage PAHO to implement the Enterprise Resource Planning Project (ERP), which will improve the economic and financial management in the Organization and the recording of transactions, reporting and preparation of Consolidated Financial Statements.

1.2. Overall Results of the Audit

- 4 We have audited the consolidated financial statements of PAHO in accordance with the International Standards on Auditing of the International Federation of Accountants (IFAC), the Audit Standards and Guidelines formulated by the United Nations Board of Auditors and the International Standards of Supreme Audit Institutions (ISSAIs).
- 5 The audit opinion confirms that these financial statements: present fairly, in all material respects, the financial position as at 31 December 2013 and the results for

the year then ended; have been properly prepared in accordance with IPSAS and the stated accounting policies; and, in all material respects, the transactions underlying the financial statements have been made in accordance with the Financial Regulations and applied to the purposes intended either by the Pan American Sanitary Conference or the Directing Council.

- 6 Our audit procedures are designed primarily for the purpose of forming an audit opinion. They included a review of the internal controls and accounting systems and procedures, only to the extent considered necessary for the effective performance of the audit. The audit work did not involve a detailed review of all aspects of PAHO's budgetary and financial information systems. Our findings therefore should not be regarded as representing a comprehensive statement of all the weaknesses which exist, or all improvements which could be made to the systems and procedures operated.
- 7 The main observations and recommendations from our audit are set out below. Our recommendations are summarized in Annex A. Follow up of actions taken by management in response to the recommendations included in the 2012 Long Form Report are set out in Annex B.
- 8 The 2013 financial statements correspond to the second year of the Spanish Court of Audit's appointment as the external auditor of PAHO.
- 9 We would like to thank PAHO for their professional and constructive approach to the external audit relationship. We trust PAHO's management keep consistently engaged with the audit process and seek to improve processes and procedures in response to our audit recommendations.

1.3. Summary of Main Findings

- 10 In this report we have commented upon the Organization's financial position, our findings with respect to Country Offices and governance matters.
- 11 Regarding Country Offices, we have noted that the internal control environment is adequate but we have drawn attention to the importance of achieving a full compliance with the IPSAS concepts, in particular, in some Country Offices.

Therefore, we recommend continuing reinforcing the training on IPSAS concepts and keeping a close oversight of those units with a higher risk.

- 12 In the Brazilian Country Office we have specifically analyzed the *Mais Médicos* Project. PAHO has set an appropriate internal control framework on this project but it is necessary to ensure compliance with its critical internal control points.
- 13 Nevertheless, we noted that there are two lawsuits against this project, and we consider prudent that PAHO set a contingency plan to face possible negative statements of both lawsuits.
- 14 The situation of the PMIS Project has greatly improved in 2013 and in the beginning of 2014. The Project has the full support of the executive level, the pre-implementation phase was completed and the phase 1 is being developed according to the estimated timetable. Phase 2 will begin in July 2014 and will finish in December 2015. In this scenario, the Project would be fully implemented on 1 January 2016. However, some critical software applications have not been purchased yet.
- 15 Since PMIS is a critical project for the organization, we encourage PAHO to keep institutional efforts to ensure the PMIS Project timetable implementation.
- 16 The Enterprise Risk Management (ERM) Project should be considered as an institutional procedure integrated into the organizational processes. However, resources devoted to the development of the ERM system may not be sufficient to implement it and to integrate it into PAHO's culture. Therefore, we encourage PAHO to make this system fully operational.
- 17 Letters of Agreement (LOAs) are a very useful tool to implement technical cooperation. Regarding LOAs management, we noticed that there are a significant number of very old LOAs, some of them even from 2004, that have not been closed yet. Therefore, we recommend that PAHO review all LOAs which are still open, close the LOAs fully implemented and request beneficiaries the final reports or the outstanding amounts to be returned to PAHO, when necessary.
- 18 Finally, we found a significant increase in the level of disbursement during the last month of the year 2013. We consider that the implementation of a relevant portion of the activities at the very end of the period involves a risk of non-compliance with sound financial management principles. In order to reduce a high

increase in the expenditure at the end of the biennium, we suggest setting an incentive to the allottees or improving the monitoring and management of the projects.

2. Financial review

19 The Director's Comments on the Financial Statements provide a comprehensive analysis of the financial performance of the Organization for 2013. We review the financial analysis provided for consistency with the information contained in the Consolidated Financial Statements and offer some further analysis to enhance the understanding of the users.

20 From our audit of the Consolidated Financial Statements we have identified several matters that we consider worth highlighting in this report:

- In the financial year 2013, the second year of the biennium, PAHO had a deficit of 2.660 USD million. It is the first time this occurred since the implementation of IPSAS in year 2010. In addition, according to the Decision of the Direction Council CD.52.R3, the total Program Budget for the Biennium 2014-2015 is expected to decrease an 8% (54 USD million¹), with no increase in the assessed contributions of the Member States for the biennium. The Secretariat of PAHO should take the necessary steps to ensure the continuity of its activities and projects improving the efficiency of the management and the degree of success in mobilizing of resources.
- During 2013, the total revenue from the Procurement of Public Health Supplies increased 6%, to 596.9 USD million as compared to 562.4 USD million in 2012. Through extensive international bidding, PAHO is able to purchase vaccines, public health supplies and equipment on behalf of Member States and international institutions at affordable prices. These revenues are the main relevant accounting line item which represents the 52% of the overall balance of revenues. The relative importance of these accounting line items did not present significant changes between 2012 and 2013.
- Revenues generated by Voluntary Contributions increased by 65% from the prior year, reaching 356.9 USD million in 2013. One of the primary sources of

¹ 563.1 USD million of Total Program and Budget in the Biennium 2013-2014, 613.4 USD million in the biennium 2014-2015

this increase was caused by the implementation of *Mais Médicos* Project, which contributed 159.8 USD million as revenue in 2013.

- Revenues also experienced an important decrease in the balance of Miscellaneous Revenue as at 31 December 2013 compared to 2012, from 20.1 USD million to negative 1.2 USD million at the end of 2013. The transfer of the PALTEX Program to PAHO resulted in the recognition of miscellaneous income in 2012 of 17.877 USD million. This recognition no longer impacts 2013 financial operations in the Organization.
- As stated in footnote 2.17 Miscellaneous Revenue includes foreign currency revaluations, exchange rate gains and losses, interest earned, realized gains and losses, and gains and losses from the sale of property, plant and equipment. Miscellaneous Revenue did not contribute significantly to the Organization this year, providing approximately 0.19% of the revenues of PAHO in 2013.
- Total revenue increased from 978.5 USD million in 2012 to 1,139.4 USD million, which is a variation of 16.4%.
- PAHO's expenses increased by 17.7% from 969.7 USD million in 2012 to 1,142.1 million as at 31 December 2013.
- Staff and other personnel costs have decreased by 0.5%, from 187 USD million in 2012 to 186 USD million in 2013.
- Procurement expenses (supplies, materials and commodities) have increased 6%, less than the percentage of total increase in expenditure. For instance, courses and seminars and travel costs have increased 41.7%, from 69 USD million in 2012 to 97.8 USD million in 2013 and contract services from 93 USD million in 2012 to 100 USD million in 2013 (7.5%). Despite the increase in this category, the 2013 duty travel expenditure was lower than in 2012.
- The disbursements in grants and transfers to counterparts have increased by 234.8%, from 43 USD million in 2012 to 144 USD million in 2013, due to the implementation of the *Mais Médicos* Project in Brazil.
- PAHO's total current assets have decreased by 88.7 USD million, from 610.4 USD million to 521.7 USD million.

- PAHO's cash balances rose by 2.9% from 160.9 in 2012 to 165.7 million in 2013. This partially offset a decrease in investments in short term (120.5 million), and an increase in the balance of Accounts Receivables - Current (27.7 million) explained by an increase in the Procurement Fund (168%). There has been a reduction of the Voluntary Contribution Funds, with the current voluntary contributions diminishing in an 8.9% and the non-current decreasing in a 31%. The reduction of Account Receivables- non Current (11.7) is explained by this decrease in the Voluntary Contributions funds.

While PAHO has sufficient resources to meet its current financial obligations (178.5 USD million in Fund Balances and Reserves, 1.79% over the figures of 2012), financial stability of the entity requires a continuous monitoring of the decrease of those assets.

- The Long Term Investments balance stands at 266.5 USD million, which should be adequate to meet PAHO needs disclosed as long term liabilities. However, total investments (long-term and short-term) decreased in 69.5 USD million from year 2012 to 2013. The decrease in the value of the investments is partially explained by the use of donor resources that were held by the Organization at the end of 2012, as some projects funded by contributions were not completely implemented at the end of 2012.
- There has been a small decrease in the value of the Inventories (8.7%). For its part, in Property, Plant and Equipment have decreased a net figure of 1.5 USD million between financial years 2012 and 2013 (1.2%).
- Employee benefits current and non-current liabilities have increased in 8%. Thus, the 187.9 USD million shown in 2012 has grown to a 203.2 USD million liability. As per IPSAS 25, this increase is consistent with the decrease of the defined benefit obligation in 9.8% (305 USD million to 275 USD million). This decrease in the actuarial valuation of the defined benefit obligation is caused by the increase in the discount rate considered in the calculation, due to the rise of interest rates in the United States.

The rise in liabilities is mostly explained by the increase in medical costs and expectations of a low return on investments due to the global economic situation. Furthermore, the value of Plan decreased (39 USD million in 2012 to 38 USD million in 2013).

In a short-term perspective PAHO has enough resources to fund the employee benefits of the staff. However, facing the future funding of this liability is a financial challenge for PAHO. For that reason we encourage going into the steps to address this challenge, over the next 3-5 years.

3. Country Offices

3.1. Introduction

- 21 PAHO is present in more than 30 countries throughout the Region of the Americas. PAHO operations and project implementation at a country level is managed by its network of Country Offices and Centers and it funds its operations using regular budget allocations as well as project funds. The cumulative disbursements by these Offices in 2013 were of about 351.7 USD million (2012: 214.4 USD million), which is a significant component of PAHO's reported activity and we, thus, carry out field visits to obtain assurance on controls over locally managed funds and expenditure.
- 22 Our selection of Country Offices is determined by a risk assessment which takes into consideration the level of expenditure, the length of time since our previous visit and discussions with Headquarters staff. We also take into consideration the recommendations of the Audit Committee and the controls performed by the Office of Internal Oversight and Evaluation Services.
- 23 During 2013 we visited the Panama, Mexico and Brazil Country Offices and the Panaftosa Center. At the end of each visit, we provided our findings and recommendations to the PWR (PAHO-WHO representative) of the Country Offices. Management has been encouraged to respond and set out a clear action plan to implement or follow up the points that we have raised. It was the fourth consecutive year that external auditors have visited the Brazil Country Office because this Office, excluding Headquarters (hereinafter HQ), is responsible for the largest proportion of PAHO's expenditure.
- 24 In addition, in the course of the fieldwork of the audit developed in HQ we have reviewed documentation regarding the activity of all Country Offices.

3.2. *Mais Médicos* Project

- 25 The participation of PAHO in the *Mais Médicos* Project derives from the *Termo de Cooperacao 80*, which was signed in April 2013 between PAHO and the Brazilian Department of Health. The aim of this project is to expand the Brazilian population's access to primary health care. In order to implement that agreement PAHO and the Cuban Government agreed the participation of Cuban doctors in the Project. The funding of the project raised 176,459,697 USD in December 2013.
- 26 We have analyzed the legal framework, the internal control procedure, the financial and the budgetary management of the *Mais Médicos* Project. In addition, we have reviewed the programming and the implementation of different transactions. We have verified the monitoring process on this project and we are aware of the changes introduced in the Brazilian Country Office's staff and in the internal control framework to reinforce them.
- 27 In our opinion, all these control measures set an appropriate internal control framework on this project. Moreover, as per the *Termo de Acordo 4*, the internal control on this project will be reinforced through a data base managed by the Brazilian PWR, which will be supported with information provided by all parties on Cuban doctors' performance. It is also expected that the Cuban Government add to this data base its own information about the Cuban doctors.
- 28 Nevertheless, it is necessary that PAHO checks the compliance of critical points of this control framework, in particular, the detailed planning of all activities linked to the project, its continuous monitoring together with representatives of the Brazilian Department of Health, the previous agreement with Brazilian Department of Health on any expense related to the project, the monthly reports from PAHO's officials on Cuban doctors activity and the new data base management.
- 29 We also noted that there are two lawsuits against this project. The first one is a lawsuit raised at the Brazilian Federal Supreme Court, which questions the constitutionality of the legal framework of the project. Currently, this lawsuit is in a preliminary stage and the Court has still not decided about the admittance of this litigation. The second one is a demand raised by a Cuban doctor to the Brazilian Labor Court for the recognition of the same labor rights than others doctors involved in the *Mais Médicos* Project.

Recommendation 1: We recommend that PAHO design a contingency plan for the *Mais Médicos* Project to face possible negative statements of both the Brazilian Federal Supreme Court, on the constitutionality of the project, and the Brazilian Labor Court, on the recognition of labor rights in Brazil for Cuban doctors. This contingency plan should include provisions to cope with the risks deriving from such negative statements (doctors' transportation, extraordinary expenses funding, liabilities, etc.).

Recommendation 2: We recommend that PAHO regularly check the compliance of the critical points of internal control framework of *Mais Médicos* Project.

3.3. IPSAS compliance

30 Under IPSAS, entities are required to recognize expenditure in the Financial Statements on an accrual basis. Although we recognize the improvement of the accrual concepts understanding and the effort made by PAHO in IPSAS training, there remains a certain level of error in its application. Thus, we have noticed some errors in the accrual expense recognition in the Mexico and Haiti Country Offices and some expenses not capitalized in the Bolivia and Haiti Country Offices.

31 The figures are not material and the percentage over the sample analyzed is low. Nevertheless, these errors justify maintaining the training of the staff on IPSAS concepts.

Recommendation 3: We recommend that PAHO continue reinforcing the training on IPSAS concepts and keep a close oversight of those units with a higher risk.

4. Governance Matters

32 There are mechanisms on which the Governing Bodies of every international organization rely to supervise the effectiveness of its activity. We have analyzed these mechanisms as part of our audit.

4.1. Pan American Sanitary Bureau (PASB) Management Information System (PMIS)

4.1.1. Background

33 The key dates in the process for modernizing the Pan American Sanitary Bureau (PASB) Corporate Management System have been the following:

- In 2008, the 48th Directing Council authorized performing an analysis for modernizing the Pan American Sanitary Bureau (PASB) named Management Information System (PMIS) Modernization Project.
- In 2010, the 50th Directing Council approved an Enterprise Resource Planning (ERP) System. The estimated budget for this project was 20.3 USD million.
- On 8th June 2011, the Director formally announced the launching of the PASB Management Information System (PMIS). The implementation schedule envisaged had two phases: Pre-implementation Phase (June 2011 – mid 2012) and Implementation Phase (mid 2012 – mid 2014).

Despite the considerable effort made by PAHO, which resulted in a number of important outputs being produced, some key elements of the pre-implementation phase were not delivered as planned and the project schedule was not achieved.

4.1.2. Status of the Enterprise Resource Planning (ERP) System

34 Throughout the year 2013, significant progress has been made in the PMIS Project: the approval and development of the Business Case; the development of a risk

assessment; the selection of the main software platform, the planning and budgeting module and the Procurement module; the selection of a company to integrate the systems and a company to support the change in management process; and the development of a communication plan and the definition of a timeline.

In addition, a new structure and a new project team were designed. The Director of Administration was appointed Executive Sponsor of the project, an External Project Manager was hired, an Internal Project Manager was assigned and the Organization established a PMIS Core Team with representatives from Technical Areas and Country Offices.

35 The estimated Project schedule is the following:

- Phase 1 (March – December 2014): Development of planning, architecture, configuration and prototype, testing and deployment of the Human Resources and Payroll areas.
- Phase 2 (July 2014 – December 2015): Development of planning, architecture, configuration and prototype, and testing and deployment of the Finance, Procurement, Planning and Budgeting areas will be developed.

Throughout this period, system integration, change management, communication plan and staff training on the PMIS system will be performed.

In this scenario, the Project is set to be ready by January 1st, 2016.

4.1.3. Source of Funding

36 The PMIS Project budget is 20.3 USD million. This amount was presented to the 2010 Directing Council: 9.2 USD million come from the Holding Account, which contained surplus funds from the 2006-2007 biennium; 9.2 USD million come from a combination of a charge against occupied posts and funds resulting from the implementation of International Public Standard Accounts (IPSAS) in 2010-2011; and 2.1 USD million come from Post Occupancy Change PMIS Funding in 2010-2011.

Of this amount, the expense already incurred has been 2.7 USD million; vendor selection process (0.6 USD million), Business Case (0.7 USD million); software application subscriptions, implementation services and change orders, external

advisor, backfill (hiring one staff in order to replace every core member team) and other expenses (1.4 USD million).

- 37 PAHO is trying to keep the project cost under the approved amount by the 2010 Directing Council (20.3 USD million). The current project cost forecast reaches 22.4 USD million, which means a difference of 2.2 USD million. The main items, among others, that are increasing the estimated budget are: ERP implementation (1.9 USD million) and backfill (assuming one staff per functional area) (1.5 USD million). On the other hand, the items of change management (0.4 USD million) and change orders and contingencies (0.5 USD million) are decreasing their estimated budget.

4.1.4. Audit Review

- 38 The situation of the PMIS Project has greatly improved in 2013 and in the beginning of 2014. The Project has the full support of the executive level, the pre-implementation phase was completed and the phase 1 is being developed according to the estimated timetable.

- 39 Nevertheless, the Treasury module has not yet been chosen. PAHO is studying different software alternatives in order to choose the best option for its treasury management, taking into account the needs to integrate the Treasury software in the software platform.

- 40 Besides, there are two software modules that PAHO wants to integrate in the software platform to support specific core functions: Procurement Tendering and the E-Learning Management System.

- 41 In our opinion, PAHO should shortly determine which software application will be selected, in order to integrate its implementation in the established schedule.

- 42 PAHO has established a PMIS Core Team which is composed of experts from each PMIS module. These core members are key staff in their respective areas. In order to mitigate the negatives effects that could arise in the regular activity of these areas, the PMIS Project budget includes an amount for hiring staff to replace every core member.

- 43 From our point of view, and taking into account the whole PMIS Project timing, it is necessary to start the backfill process and to hire staff in order to avoid that the functioning of the different areas is affected.

- 44 We consider that compliance with the PMIS Project implementation schedule is a critical issue for the Organization. As we described in our last report, some of the current software applications used by the Organization are outdated and unable to support the information and financial statements based on IPSAS, since they do not have the capabilities to duly obtain reports and information in an efficient manner. This results in a complex and difficult process for preparing the financial statements, which needs manual operations and off system adjustments (depreciation of assets, accruals, capitalization of tangible and intangible assets, etc.).
- 45 To this respect, we noticed several errors in these off-system works and calculations and in some accounting entries, which do not however affect the representativeness of the Financial Statements. As a consequence, these outdated systems are still a risk for the Organization. Therefore, it would be very desirable for the PMIS system to be installed and operational in the 2016-2017 biennium.
- 46 Furthermore, the delay in the PMIS system implementation will increase the budget, which is already exceeded.

Recommendation 4: We recommend deciding the software modules that need to be purchased and their integration in the PMIS Project timeline.

Recommendation 5: We recommend beginning the backfill process and hiring staff in the areas which have temporarily lent their key staff to the PMIS Project.

Recommendation 6: We recommend that PAHO focus its efforts in order to comply with the estimated deadline.

4.2. Enterprise Risk Management

4.2.1. Background

- 47 The key milestones in the process for creating a risk management framework have been the following:
- In 2011, a framework based upon ISO3100, a standard that provides principles and guidelines on risk management, was adopted.

- In November 2011, the Senior Risk Management Committee was established and its first meeting took place in November 2012.
- In 2012, the Enterprise Risk Management Policy was approved, communicated and included in the PAHO/WHO E-Manual.

4.2.2. Status of the Enterprise Risk Management

48 According to the Strategic Plan 2014-2016, PAHO will apply its Enterprise Risk Management (ERM) framework to identify the risks and to implement mitigation measures that increase the likelihood of achieving the expected results. The Risk Management methodology was included in the Biennium Work Plan 2014-2015 Operation Planning Guidelines.

49 Throughout the year 2013, PAHO only performed four risk assessments in Country Offices and two training workshops on this matter.

50 Despite the aforementioned background, the implementation of the system continues relying upon the efforts of only one key staff member. Besides, this staff member is close to his retirement age, in August 2014.

51 ERM has been funded with extra budgetary funds that were provided to PAHO for this purpose. This funding will expire in July 2014.

4.2.3. Audit Review

52 In our opinion, the following issues should be addressed shortly:

- The resources devoted to the development of the ERM system may not be sufficient to achieve, among others, the next goals: to complete the risk register and risk profile in the whole Organization; to update the entity risk maps in order to prioritize key risks for each area or country office; and to implement a plan to improve the risk management capabilities. Funding of ERM should be sufficient in order to reach its aims and to be integrated into PAHO's culture.
- The approval of the document PAHO Top Corporate Risk.

- The replacement of the staff member in charge of the ERM. His relevant duties and experience imply the need to prepare an adequate handover between him and his/her substitute. Otherwise, a loss of information will occur and this may, subsequently, cause disruption in ERM development.

Recommendation 7: In order to ensure success when the system to be fully operational, we recommend that PAHO create a Risk Management Unit to develop the management risk functions and to review the resources devoted to the fully development and maintenance of the Enterprise Risk Management.

4.3. Letters of Agreement

- 53 Letters of Agreement (LOAs) are a very useful tool to implement technical cooperation. Therefore, since a big part of PAHO's activity is channelled through LOAs, a continuous monitoring is necessary. PAHO carries out this monitoring but we noticed some deficiencies in this control.
- 54 First of all, we observed that there is a significant number of very old LOAs with end dates even from 2004 that have not been closed yet. For instance, from 1.1.2008 to 12.31.2011 there are more than two hundred LOAs which should be closed but remain open. Moreover, there is no information on AMPES/OMIS about the reason why those LOAs have still not been closed. Therefore, PAHO HQ does not know the specific reasons for this situation, which entails a weakness in the control of these LOAs.
- 55 In addition, the current policy on LOAs sets the deadline for the beneficiary to submit the final report to PAHO (sixty days after the final date of the agreement), but this policy does not set a deadline for closing the LOAs.
- 56 Moreover, we noticed that in several LOAs the beneficiaries have still not returned the unexpended funds to PAHO which entails a risk of financial loss.
- 57 Even though PAHO has made an extraordinary effort to review the LOAs policy, there is a risk that LOAs could be used instead of service contracts or for other purposes than those for which they were created if this new policy is not approved.

58 The improper use of LOAs remains a risk, specifically when LOAs are used instead of service contracts, because it might be a way of avoiding competitive bidding.

Recommendation 8: We recommend that PAHO review all LOAs still open with ending dates older than a year. After this review PAHO should determine the status of each LOA and should close LOAs totally implemented and request from the beneficiaries the final reports or the outstanding amounts to be returned to PAHO, when necessary.

Recommendation 9: We recommend that PAHO set deadlines for closing LOAs after their ending date.

Recommendation 10: We recommend that the E-Manual and the new policy to be approved define the exclusions for the use of LOAs in a clearer way in order to avoid the misuse and the misunderstanding of this valuable cooperation instrument. We suggest the limits and differences between service contracts and LOAs be clarified.

4.4. Increase of expenses at the end of the budgetary period

59 PAHO Regular Budget includes the Member States' Assessed Contributions, Miscellaneous Revenue and the PAHO implemented resources from the WHO Regular Budget Allocation in order to implement the international health programs established by the World Health Assembly for the Region of the Americas.

60 As a result of analysis from a time perspective of the disbursements funded by Regular Budget² (both PAHO Regular and WHO funds), we found a significant increase of the level of disbursement in the last month of the year 2013.

61 Thus, eliminating the effect of expenses directly linked to Human Resources (payroll and some expenses of the Staff Health Insurance), we found that the disbursements of December (6.3 USD million) were a 194% higher than the

² Regular Budget Funds, as they are defined in the accounting records, excluding expenses funded by other sources such as Revolving Funds or Voluntary contributions among other sources of funding.

average level of the expenditure of the first eleven months of the year (2.14 USD million), under homogenous criteria.

- 62 It has to be admitted that, from an economic point of view, all the budget-basis organizations tend to increase their expenditure at the end of the budgetary period. PAHO is not an exception and, consequently, we noticed that the closure of the biennium pushes the Areas Directors and the PWRs to consume their resources in order to meet their aims.
- 63 However, we do not considered that the implementation of a relevant portion of the activities at the very end of the period to be a good practice to reach the programmatic objectives of the biennium in an efficient manner. Therefore, we consider that there could be a risk of not obtaining the best value for money.
- 64 Therefore, taking into account that the total amount of the biennium 2014-2015 budget is lower than the 2012-2013 one, as well as the commitment of the Secretariat to be more efficient in its management, it is necessary to take all the necessary steps to encourage every single manager to improve the efficiency in their planning and management.
- 65 Currently, the budget policy allocates all the unexpended regular budget resources to replenish the Working Capital Fund. Any excess of the authorized level of the Working Capital Fund is considered a revenue surplus and is used to cover subsequent needs of resources, once the Director, advised by the Subcommittee of Planning and Budget, appreciates those needs. The reach of the programmatic objectives and the financial execution of the budget is monitored on a semester basis.

Recommendation 11: We recommend setting an incentive to the allottees who reach their programmatic aims with the highest level of efficiency, allowing them to reuse a portion of the saved funds in the following biennium.

Recommendation 12: We recommend improving the monitoring and the planning of the projects funded with regular budget in both financial and programmatic side to avoid the accumulation of expenses at the end of the biennium.

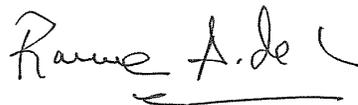
5. Follow up of prior year recommendations

- 66 In our report for 2012, we made a number of recommendations about PAHO's management. As part of our work we have followed up the progress that PAHO has made in implementing these. The detailed follow up, including both the response from PAHO and our comments thereon, is set out in Annex B.
- 67 Overall, we are of the opinion that PAHO has responded appropriately to our previous recommendations and is taking steps to address the issues raised. We conclude that PAHO has responded very positively to our recommendations, since most of them have been closed or in progress. We took note of the implementation of our recommendations on PMIS since this project is critical to the Organization. However our recommendations on ERM are not completely implemented.

Acknowledgement

- 68 We wish to record our appreciation for the co-operation and assistance provided by the Director and the staff of the Organization during the course of our audit.

Madrid, April 11, 2014



Ramón Álvarez de Miranda García

President of the Spanish Court of Audit

Annex A - Summary of Audit Recommendations

Recommendation 1: We recommend that PAHO design a contingency plan for the Mais Médicos Project to face possible negative statements of both the Brazilian Federal Supreme Court, on the constitutionality of the project, and the Brazilian Labor Court, on the recognition of labor rights in Brazil for Cuban doctors. This contingency plan should include provisions to cope with the risks deriving from such negative statements (doctors' transportation, extraordinary expenses funding, liabilities, etc.).

Recommendation 2: We recommend that PAHO regularly check the compliance of the critical points of internal control framework of *Mais Médicos* Project.

Recommendation 3: We recommend that PAHO continue reinforcing the training on IPSAS concepts and keep a close oversight of those units with a higher risk.

Recommendation 4: We recommend deciding the software modules that need to be purchased and their integration in the PMIS Project timeline.

Recommendation 5: We recommend beginning the backfill process and hiring staff in the areas which have temporarily lent their key staff to the PMIS Project.

Recommendation 6: We recommend that PAHO focus its efforts in order to comply with the estimated deadline.

Recommendation 7: In order to ensure success when the system to be fully operational, we recommend that PAHO create a Risk Management Unit to develop the management risk functions and to review the resources devoted to the fully development and maintenance of the Enterprise Risk Management.

Recommendation 8: We recommend that PAHO review all LOAs still open with ending dates older than a year. After this review PAHO should determine the status of each LOA and should close LOAs totally implemented and request from the beneficiaries the final reports or the outstanding amounts to be returned to PAHO, when necessary.

Recommendation 9: We recommend that PAHO set deadlines for closing LOAs after their ending date.

Recommendation 10: We recommend that the E-Manual and the new policy to be approved define the exclusions for the use of LOAs in a clearer way in order to avoid the

misuse and the misunderstanding of this valuable cooperation instrument. We suggest the limits and differences between service contracts and LOAs be clarified.

Recommendation 11: We recommend setting an incentive to the allottees who reach their programmatic aims with the highest level of efficiency, allowing them to reuse a portion of the saved funds in the following biennium.

Recommendation 12: We recommend improving the monitoring and the planning of the projects funded with regular budget in both financial and programmatic side to avoid the accumulation of expenses at the end of the biennium.

Annex B - Implementation of Prior Year Recommendations

We reviewed management’s implementation of recommendations made in our prior year long form report. We have summarized the response and provided our evaluation, based on the audit work we have undertaken in respect of internal controls.

RECOMMENDATION	MANAGEMENT RESPONSE	SCA COMMENT
<p>Recommendation 1</p> <p>Consequentially, and given the important monetary amount of those operations, we recommend that PAHO consider the possibility of hedging the exchange rate risk. PAHO, as advised by the Investment Committee, might consider, among others, the following options to address the exchange rate risk:</p> <ul style="list-style-type: none"> ▪ The use of financial derivatives (forwards, collars, cap, floor) to hedge exchange rate risk. ▪ Investing locally in case the investments comply with the conservative investing policies of the organization. We encourage keeping a prudent investment policy. ▪ Increasing temporarily the local currency balances, in order to minimize the currency exchange risk. 	<p>The Investment Committee reviews the policies concerning the management of foreign currency and continues to monitor the risks associated with the various country office operations. Various proposals have been submitted to Executive Management over the past five years, including investing locally to limit the need to enter into the foreign exchange markets, and hedging opportunities. Executive Management has reviewed the feasibility of hedging large scale foreign currency requirements. However, it was determined that, except for purchases that require payment in foreign currencies not held, there is no economic benefit to hedging foreign currency requirements at this time. The Committee is revisiting the proposal to invest locally so that projects that receive funds in local currency that will eventually be disbursed in local currency are not impacted by market transactions. The Committee met with Citibank to explore the investment options that are within the Investment Guidelines.</p>	<p>IN PROGRESS</p>
<p>Recommendation 2</p> <p>We recommend that the E-Manual define exclusions for the use of letters of agreement in a clearer way in order to avoid the misuse and the misunderstanding of this valuable cooperation instrument. We suggest to specify what services should be excluded from the use of letters of agreement and to establish control mechanisms to make sure this is observed.</p>	<p>A review of the Letter of Agreements (LOA) Policy is underway. This review has been done in coordination with the Office of Legal Council (LEG) and the Department of Financial Resources Management (FRM). The revised policy is currently proceeding through the mandatory review of the E-Manual Standing Committee. Among other things, the new proposed policy clarifies the section related to exemptions from the use of LOA to avoid misunderstandings. Once the new LOA policy is approved, FRM and LEG will assess how to improve the existing controls.</p>	<p>IN PROGRESS</p>

RECOMMENDATION	MANAGEMENT RESPONSE	SCA COMMENT
<p>Recommendation 3</p> <p>In order to have a better understanding and control of the category of “Courses and seminars”, they should be channeled through Letters of Agreements if they are carried out by external entities or through service contracts if they are carried out by PAHO and for PAHO staff. Therefore, we recommend PAHO to reconsider the current concept and regulation of this important category.</p>	<p>FRM Country Accounting Services Team put in place some controls on Courses and Seminars to standardize the process in the country offices which includes standard form for institutions to request PAHO contributions, budgets, evaluation of the activities performed.</p> <p>Furthermore, the Department of Information Technology Services (ITS) developed a workflow that will separate the Courses and Seminars activities in accordance with the recommendation raised by the External Auditor. Either, funds are transferred to counterpart institution (similar treatment to the LOA process) or activities where PAHO organizes and maintains control of the funds, the coordination of activities, contracts and purchases and disbursement of funds are performed in-house. This initiative will be implemented in PWR-BRA as a pilot program.</p> <p>FRM and the Office of Internal Oversight and Evaluation Services (IES) participated in several workflow discussions with ITS (March 2013) and provided information on controls required within the workflow to ensure accountability.</p> <p>This recommendation should be closed.</p>	<p>CLOSED</p>
<p>Recommendation 4</p> <p>We recommend using a more open selection process with, at least three offers, as it is established in the PAHO procurement process. In those cases in which there is only one candidate because of the high specialization required, this should be clearly justified.</p>	<p>The title Contractual Service Agreement (CSA) was eliminated in 2011.</p> <p>Regarding the Sole Source contracts in the Organization, the E-manual states the following:</p> <p>30 The Director of Administration or his/her authorized representative, in accordance with PAHO/WHO E-Manual Chapter VI.5.3, may determine exceptions to the competition rule in the following circumstances:</p> <ul style="list-style-type: none"> ▪ When there is no competitive marketplace for the goods and services, such as where a monopoly exists, where prices are fixed by legislation or government regulation or arrangement, or where the requirement involves a proprietary product or service; ▪ When the equipment and supplies must be compatible with other standardized equipment and supplies; ▪ When PAHO can benefit from an existing agreement entered into by another agency of the UN system and the contractor has agreed to offer the goods or services to PAHO on the same terms; ▪ When, at PAHO Headquarters, the goods or services are available through a method of supply developed by United 	<p>CLOSED</p>

RECOMMENDATION	MANAGEMENT RESPONSE	SCA COMMENT
	<p>States of America Federal Agencies and Departments;</p> <ul style="list-style-type: none"> ▪ When offers for identical goods and services have been obtained competitively within a reasonable period, usually not greater than 12 months, and the prices and conditions offered remain competitive; ▪ When, within a reasonable prior period, a formal solicitation has not produced satisfactory results; ▪ When the goods and services are for a PAHO declared emergency, in accordance PAHO/WHO E-Manual Chapters VII.3.4; ▪ When the value of the procurement is below the established monetary thresholds, as indicated in the Practitioner’s Handbook; ▪ When it is determined by PRO that there is one source of supply for a good or service, as described in the Practitioner’s Handbook; ▪ Other compelling and exceptional reasons, where competitive bidding will not be in the best interest of PAHO. ▪ The report mentioned in paragraph 37 shows 236 purchases of which 93 are purchases for less than US\$5,000 (no competition needed as per PAHO Regulations and Rules); <p>12 purchases are based on Long Term Agreements (LTAs), which are based on competitive processes; 4 purchases are related to the General Service Administration (GSA) vendors, already competed by GSA; 7 purchases are UN (already competed by UN agencies); 4 purchases are copyright; 2 purchases are monopolies; and, 2 purchases are repeated orders.</p> <p>That represents a total of 124 purchases which did not need bidding process in accordance with PAHO Regulations.</p> <p>The majority of the other 112 purchases represent contracts with individuals and companies with unique characteristics. Each file has an adjudication report.</p> <p>Furthermore, the Department of Procurement and Supply Management (PRO) always requests that the Purchase Authorization (PA) includes a justification in case sole source is requested.</p> <p>This recommendation should be closed</p>	
<p>Recommendation 5</p> <p>We recommend that PAHO continue reinforcing the training on IPSAS concepts and keep a close</p>	<p>FRM will continue to reinforce the understanding on IPSAS concepts through Elluminate sessions with country offices</p>	<p>IN PROGRESS</p>

RECOMMENDATION	MANAGEMENT RESPONSE	SCA COMMENT
oversight of those units with a higher risk.	during the fourth quarter of 2013. A document detailing lessons learned from the 2012 financial closure exercise will be provided to the country offices during the second quarter of 2013.	
Recommendation 6 We recommend that PAHO focuses its efforts in order to comply with the estimated deadline in the pre-implementation phase as a priority issue. That phase is the most important as it defines the comprehensive change management and the structure of the whole ERP project.	PAHO is presently carrying out the pre-implementation phase and agrees that this is an important phase of the ERP. Priority has been given to maintain the scheduled timeline for the ERP implementation.	CLOSED
Recommendation 7 We recommend that PAHO increase its communication and information actions through all levels of the Organization. It is necessary for the staff to be informed about the project progress, its advantages, benefits and cost, and the training to be planned well in advance.	PAHO will issue an RFP to engage a vendor specialized in ERP communications and change management. Due to the importance, impact and sensitivity of the project, it is imperative to adopt the most appropriate communication channels for this project and to use the support of an experienced partner.	CLOSED
Recommendation 8 We recommend beginning the necessary analysis to determine the steps to take in the coming first and second phases. PAHO should define indicators or targets in order to enable monitoring the progress in ERP's implementation.	This will be laid out in the PMIS Project Plan, which will be reflected in the 2014-15 BWP of ITS and AM/SI.	CLOSED
Recommendation 9 We recommend that the PAHO's Director should define the Risk Management as an institutional process, thus demonstrating the commitment, the support as well as the importance of this project within the whole Organization.	This is stated in the ERM Policy that has just been published in the PAHO/WHO E-manual Chapter I.6.5b on 17 May 2013. This recommendation should be closed.	CLOSED
Recommendation 10 We recommend that the Draft Risk Management Policy be adopted as soon as possible.	This is stated in the ERM Policy that has just been published in the PAHO/WHO E-manual Chapter I.6.5b on 17 May 2013. This recommendation should be closed.	CLOSED
Recommendation 11 We recommend that PAHO create a Risk Management Unit to develop the management risk functions and review the resources devoted to the implementation and maintenance of the system to ensure success when the system will be fully operational.	AM has an Enterprise Risk Management professional now, who is training and facilitating the creation of Risk registers and Risk mitigation plans in countries and HQ. The requirement for additional Human Resources to form a unit will be weighed against the response of the Countries and HQ entities to the ERM training.	NOT IMPLEMENTED YET
Recommendation 12 PAHO needs a comprehensive E-Manual to provide guidance and assistance to all staff in the implementation of the PAHO values of equity, excellence, solidarity, respect and integrity. We recommend that PAHO proceed to update the E-Manual with all policies and procedures involve in PAHO's management	The PAHO/WHO E-Manual adopts the WHO E-Manual table of contents in its entirety, except where PAHO has a policy variance from the WHO. For both types of policy (variances, making up about 40% of all policies and non-variance, making up about 60%) the PAHO/WHO E-Manual, has been completed since 18 June 2012 (GIB:HQ/FO-12-49). Effective from 18 June 2012, the	IN PROGRESS

RECOMMENDATION	MANAGEMENT RESPONSE	SCA COMMENT
	<p>PAHO/WHO E-Manual has been and remains the only repository of PAHO policies. Therefore, a comprehensive electronic PAHO/WHO E-manual is available via the PAHO Intranet for all personnel and managers. Further, the PAHO/WHO Standing Committee usually meets monthly to review draft policies. Since June 2012, the Standing Committee has cleared about 1-2 policies a month for publication in order to improve policies and keep the manual current.</p> <p>With respect to procedures, a modality and work plan for improved handling and updates to procedures, when required, is being developed to coincide with the PAHO Management Information System's (PMIS) implementation. Doing so avoids duplication of work and achieves economies as many of the standard operating procedures now handled manually will be automated and/or impacted by the workflows of PMIS.</p>	
<p>Recommendation 13</p> <p>Due to different valuation of the PALTEX Program inventory and the concern that it would contain obsolete, damaged or lost books, we recommend PAHO to carry out a physical inventory control by an independent party.</p>	<p>PAHO is preparing the RFP requesting bids from accounting firms to conduct an independent physical control of PALTEX inventory. Mr. Eduardo Castro will be the project officer for this initiative and with the support of FRM, will ensure completion of this task by the fourth quarter of 2013.</p>	<p>IN PROGRESS</p>
<p>Recommendation 14</p> <p>We consider that PAHO should strengthen the control over the books inventory. Currently, all the operations are registered manually by the PALTEX staff by means of software program. We recommend the use of electronic control systems, using bar code reader that provides accurate information about the inventory.</p>	<p>The module needed an electronic bar coding reader which was bought in April 2013. Additional programming is needed in order to support this module.</p> <p>We expect to test the module in the third quarter of 2013. If everything is working appropriately, it will be implemented in some distribution Centres in 2014.</p>	<p>IN PROGRESS</p>
<p>Recommendation 15</p> <p>We suggest that PAHO perform a study on the technical and economic future viability of PALTEX Program. In addition to analyzing whether the revenues obtained cover expenses for operation, the Organization should analyze the increasing consumption of digital media versus traditional publishing.</p>	<p>A study on the Technical and economic viability will be performed the first quarter of 2014.</p> <p>PAHO will also analyze the use of eBooks and digital data versus hard copies.</p>	<p>IN PROGRESS</p>