

## Certification of Financial Statements

**The Financial Statements and supporting Notes are approved:**



**Michael H. Lowen**

**Manager**

**Area of Financial Resources Management**



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**Director**

**Pan American Health Organization**

**05 April 2013**

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## **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 evaluation of the status of implementation of the biennial workplan.

## **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 2012 through 31 December 2012, 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), Personnel Rules, the E-Manual and the Manual for Country Office Operations, 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 Office of Internal Oversight and Evaluation Services, the Ethics Office, the Office of Legal Counsel, the Country Focus Support Office, the Area of Planning, Budget and Institutional Development, the Area of Human Resources Management, and the Area 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 PAHO Infrastructure Investment Projects Committee (PIIC), the Investment Committee, the Disaster Task Force, and the Epidemic Alert and Response Task Force.

## **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 (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 2012 through 31 December 2012, the Auditor General has concluded the following:

*“Based on the findings of its oversight activities in 2012 and in previous years (and also taking into account the findings of other sources of assurance), IES's overall opinion is that PAHO's internal control environment provides reasonable assurance on the accuracy, authorization and timely recording of transactions, assets and liabilities, and on the mitigation of risks to the achievement of the Organization's objectives. Absolute assurance is, of course, impossible, as internal controls have inherent limitations. The degree of compliance with internal controls may deteriorate (or improve) over time, and a range of factors (including error, fraud, and changes to conditions and internal procedures) may render some internal controls inadequate. As a consequence, the dynamism of the Organization's activities and its changing risk profile pose a continuing challenge to the efficiency and effectiveness of internal controls. To strengthen PAHO's internal control environment, and thereby bring it beyond its current adequate status to a more satisfactory level of rigor and transparency, IES draws attention to three inter-related areas for improvement. IES advises management to make internal controls less manual in nature; more clearly to link internal controls to risks; and more explicitly to define and formalize internal controls. ”*

The Areas of Financial Resources Management (FRM) and Planning, Budget and Institutional Development (PBI) 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 the 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.

The Director of Administration initiated the deployment of a conceptual framework to implement an Enterprise Risk Management program for PAHO in 2011. PAHO's approach to risk management is an integral and systematic process not represented by a static risk register, but by a process that is continuously identifying, mitigating, monitoring, and communicating top risk events to the Organization. This type of process requires a risk management framework, a risk governance policy, a risk assessment methodology, and Organization-wide training before comprehensive risk assessments can be performed. The completion of the comprehensive risk assessments will then form the foundation of a factual and accurate risk register.

In 2011, PAHO's Executive Management team approved the conceptual framework of the ERM, which is based upon ISO31000. Subsequently, the Office of Administration (AM) conducted risk assessments to test the methodology designed to ensure it was appropriate for the Organization. The Director of Administration approved the methodology to be employed, conducted additional risk assessments at the strategic and operational levels, and published a preliminary risk register in 2012.

AM has also taken action to purchase and implement a Risk Management Information System that will be used to support the overall ERM effort in the Organization. This system was implemented in December 2011 and is fully functional. Furthermore, as part of the governance structure of ERM in PAHO, a senior risk committee has been established, comprised of officials from those Areas with primary risk identification and mitigation responsibilities. The committee convened in November 2012 and finalized recommendations on the Top Corporate Risks to be managed at the headquarters level. This organizational risk register will be presented to the Director in 2013 for final approval.

## 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, 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 of the Office of Internal Oversight and Evaluation Services (IES) 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 and evaluating the effectiveness and efficiency of organizational governance, internal controls, operations, and processes. IES undertakes internal audit and evaluation 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.

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 March and October of 2012.

The system of internal control has been in place for the year ending 31 December 2012 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
<p><b>1. Corporate Administrative Systems -</b></p> <ul style="list-style-type: none"> <li>The implementation of International Public Sector Accounting Standards (IPSAS) has further highlighted the weaknesses in the collection of legacy systems, which required significant modification and manual "work arounds" to meet the requirements of accrual accounting, asset capitalization and depreciation, and annual financial reporting. Furthermore, the systems cannot easily provide the range of integrated management reporting required of a dynamic and growing Organization.</li> <li>The implementation of an Enterprise Resource Planning (ERP) system, which would integrate Program Planning, Budget, Finance and Human Resource administration, will result in more accurate and comprehensive real-time information. However, it will also require an increased level of interaction with the ERP by all staff, providing accurate data and extracting necessary information in a decentralized environment. Given that the current systems are not fully integrated, much of this work is centralized at the Regional Headquarters. Therefore, the required</li> </ul>	<ul style="list-style-type: none"> <li>The PAHO Management Information System (PMIS) team is in the process of selecting the ERP software and systems integrators. We anticipate that final selections will be made by June 2013. The specific implementation of modules will be determined after consultation with the selected system integrator with the aim of deploying the system in 2015.</li> <li>The Financial Accountability Framework as implemented by the Area of Financial Resources Management monitors the basic controls in the country offices to ensure compliance with Financial Regulations and financial policies. The risk-based planning approach employed by the Office of Internal Oversight and Evaluation Services also provides feedback regarding the operations of the various offices. Training on specific finance topics (e.g.</li> </ul>

<p>competencies to fully realize the effectiveness of an ERP do not exist throughout the Organization.</p>	<p>accrual accounting) is continuously provided for the country office staff. Included in the implementation plan for the ERP will be a Change Management and Communication Plan which will help to identify and communicate the technical updating requirements of the various categories of staff throughout the Organization. A comprehensive Training Plan will be developed that combines training regarding the ERP requirements and capabilities, as well as technical competencies needed to meet the control requirements, whether financial, budgetary or administrative.</p>
<p><b>2. Project Implementation -</b> 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>	<ul style="list-style-type: none"> <li>• The Organization continues a systematic, coordinated review of Voluntary Contributions proposals, which includes corresponding inputs from country-based colleagues, as well as regional technical and administrative personnel. Processes are underway to implement an ERP which will facilitate improved monitoring of Voluntary Contributions' implementation. During 2011, the Area of Planning, Budget, and Resource Coordination implemented an online tool to identify Voluntary Contributions' coordinators with a view toward increasing accountability and coordination.</li> <li>• In addition, an assessment of the Voluntary Contributions Management Function was conducted in 2012 resulting in key recommendations for improvement, including definition of a policy framework, improvements in organization structure and better definition of roles and responsibilities, development of guidelines for management of Voluntary Contributions, among others. As part of the recommendations, a Resource Coordination Committee was established, with the participation of Senior Managers, including technical areas, AM, External Relations, Resource Mobilization and Partnerships, and PBI. The Resource Coordination Committee meets on a quarterly basis. Through improved clarity on the Voluntary Contributions Management Function and the implementation of the recommendations of the assessment, greater accountability for Voluntary Contributions implementation is anticipated.</li> </ul>
<p><b>3. Succession Planning -</b> The imminent retirement of a significant proportion of senior managers has the potential to result in a loss of institutional knowledge.</p>	<p>The Organization is actively engaged in succession planning through the Human Resources Management biennial HR Plan for each PAHO entity, which requires the managers to plan for retirements and other staffing requirements. Furthermore, all senior managers are required to submit an "end of mission" report prior to changing roles, transferring to another United Nations organization, or retiring.</p>
<p><b>4. Emergency Response</b> PAHO, as the preeminent health agency in the Region of the Americas, must take a leadership role in addressing</p>	<p>PAHO has adopted an institutional response and disaster policy with the objective to mobilize the entire organization in case of major disasters. That policy requires the Organization to have</p>

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<p>emergencies. The impact and severity of recent emergencies in the Region, including the H1N1 crisis and the disaster in Haiti, have highlighted the need to have a strong, centralized team of specialists to analyze and coordinate response requirements and information.</p>	<p>an Emergency Operations Center (EOC), which centralizes all information, coordinates and controls all PAHO/WHO health-related response operations during emergencies, major epidemics and disasters. In order to meet the longer-term needs of the Organization and the region, an Emergency Operations Center has been established and has been operational since September 2012.</p>
<p><b>5. International Economic Environment -</b>  The prolonged challenging global economic environment presents several risks to the Organization's ability to fund the Regular Budget:</p> <ul style="list-style-type: none"> <li>• Member States have continued to espouse a policy of zero to minimal nominal growth to the Regular Budget as a result of their own fiscal challenges.</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 the Regular Budget resources locally.</li> </ul>	<p>The Organization has a very conservative Investment Policy overseen by the Investment Committee. The Investment Committee meets in person at least twice each year. The Investment Committee 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 with four investment managers to manage approximately \$200 million of the \$600 million portfolio, thus taking advantage of expertise, economies of scale and opportunities in the market.</p> <p>The Organization continues to monitor 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 Regular Budget is denominated in US dollars, fluctuations in local exchange rates will still impact the country office's "buying power". Country Offices work closely with the Area of Planning, Budget and Institutional Development to address these issues.</p>
<p><b>6. Funding of Long-Term Employee Liabilities -</b>  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 comprehensive plan to fully fund the ASHI liability over a determined period of time.</p>	<p>The Director has approved a payroll surcharge to begin the funding of the significant liability attributable to After-Service Health Insurance benefits for current and future retirees of the Organization. In 2012, this surcharge provided \$1.9 million in revenue to the ASHI Trust. Investment income contributed another \$0.6 million to the ASHI Trust. The Pan American Sanitary Conference approved the transfer of \$10 million from the surplus generated from the implementation of IPSAS. However, in order to fund the liability over the next 30 to 40 years, additional consistent funding sources must be identified. The Organization has contracted with an actuarial firm to provide an analysis of the various options to meet this funding requirement. This comprehensive plan will be presented to the PAHO Governing Bodies for consideration in 2013. Furthermore, the Investment Committee is in the process of requesting proposals for the external management of the ASHI Trust, to maximize the income to the Trust based on the long-term nature of the underlying liability.</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 2012 through 31 December 2012, and remains so on the date I sign this statement.

A handwritten signature in dark ink, appearing to read 'Carissa F. Etienne', written over a horizontal line.

**Carissa F. Etienne**

**Director**

**Pan American Health Organization**