

SPC/CRGA 48 (2018)

Paper no. 7.3
ORIGINAL: ENGLISH

**FORTY-EIGHTH MEETING OF THE
COMMITTEE OF REPRESENTATIVES OF GOVERNMENTS AND ADMINISTRATIONS**
(26–28 June 2018, Noumea, New Caledonia)

AGENDA ITEM No. 7: Audit and Risk Committee Report

(Paper presented by the Secretariat)

Purpose

1. This paper presents the report prepared by the SPC Audit and Risk Committee (ARC) to update CRGA 48 on the Committee's work over the past 12 months.

Recommendations

2. CRGA is invited to:
 - i. note the report from the Chair of the Audit and Risk Committee;
 - ii. approve the proposed amendments to the ARC and Internal Audit Charters.

Background

3. The ARC has met three times since CRGA 47: in November 2017, and in March and June 2018.
4. Mr Savenaca Narube resigned as a member of the committee earlier in the year and Ms Caren Rangi was subsequently appointed to the committee in May 2018. Ms Rangi is a Cook Islander, resident in New Zealand. She has outstanding qualifications and her appointment is warmly welcomed by the committee.

Financial viability and sustainability

5. At its June meeting ARC received a report on SPC's financial performance to end April 2018 and an early working draft of the budget for 2019. The details of SPC's financial performance will be covered separately on the CRGA agenda. But ARC has noted, with increasing concern, SPC's financial vulnerability. The committee believes this is the greatest risk facing the organisation.
6. Over recent years, including with very strong efforts since CRGA 47, SPC has taken a number of difficult decisions to strengthen the organisation's financial situation through better expenditure management by prioritising programmes and activities, improving administrative efficiencies, reducing staff costs wherever possible, and generally strengthening the efficiency of the organisation. It has also taken steps to improve revenue through improved project execution and a focus on increasing the overall level of project management fees. All these things have been done while ensuring that the organisation can continue to meet the needs of member countries and maintaining its services and support to the region.
7. Despite these measures, SPC's financial situation remains vulnerable and ARC considers the outlook unsustainable. There are a number of contributing factors, the most glaring of which is the shortfall in assessed contributions. Arrears in member contributions, including host country grants as at the end of May amount to EUR 5.8 million. If all members were meeting their obligations in full and in a timely way, SPC would be in a position to provide greater support to the region, and build greater financial resilience and strengthen reserves.
8. ARC has addressed two questions – does SPC need additional resources and, given its track record and its performance, does it deserve greater resources? Other papers on the CRGA agenda provide further details relevant to these questions. But given its mandate, which includes identifying, assessing and reporting to CRGA on the risks faced by the organisation, ARC has a responsibility to do what it can to ensure these issues are fully understood.

Internal audit work plan

9. The international accounting and audit firm, PricewaterhouseCoopers, (PwC), has been appointed to undertake the internal audit work programme as approved by the ARC. The Committee approved three areas for review and investigation in 2018 – Grant Management, Business Continuity and a review of the Finance Procedures Manual.
10. ARC received PwC's report on Grant Management at its June meeting. The committee agreed that the report has identified areas where SPC needs to make further improvements to ensure its policies and practices are best practice. These include updating its grant policies and strengthening the capacity of

the organisation to ensure project management includes a strong emphasis on effective grant management where this is part of the project scope. SPC management will consider these issues in further detail and submit new policies and procedures for ARC's approval in due course.

11. PwC has also provided a framework for addressing and strengthening business continuity arrangements for SPC. ARC has agreed that this is an area of priority. The first phase of the work will be to identify operational risk exposures and conduct a business impact assessment on all processes. This work will be completed before the end of 2018. Business continuity is a potentially very large issue with organisation-wide implications and, almost certainly, resource implications.
12. ARC has also identified the issue of data security as a priority for the internal audit work plan and it is anticipated that PwC will be asked to review these issues and make recommendations for improvement, hopefully with the work being undertaken in 2019.
13. SPC staff have continued to review critical policies as part of the overall work plan. These have included revised policies for Travel, Credit Card Use, Cash Management and Privacy.

2017 Audited financial statements

14. In line with the committee's mandate under the ARC charter, ARC met with SPC's external auditors, KPMG, at its meeting in June 2018. The committee noted with satisfaction that SPC has again received an unqualified audit opinion from the external auditors on the organisation's 2017 financial statements.
15. The transition of SPC to the IPSAS¹ accounting and reporting platform has been essentially completed with these 2017 accounts.
16. As part of the external audit process, and in line with standard practice, KPMG provided SPC with a Management Letter raising a small number of matters the auditors considered SPC needed to review. The most important of these were the performance of SPC's Provident Fund and the issue of non-exemption by Fiji of VAT in a number of areas that would normally be covered under the host country agreement. SPC management has undertaken to examine the matters raised by the auditors and will report back to ARC at a future meeting. These matters do not have any material bearing on the financial statements and do not impact on the audit opinion.

Systems upgrades

17. ARC continues to monitor progress with the development and implementation of three projects designed to improve SPC's key operational procedures:
 - i. Jobs module – to enable the finance system to track and report on project funding and to provide SPC's project managers with financial and timekeeping tools to effectively plan, execute and monitor their projects;
 - ii. HR system project – to improve efficiency in the management of SPC's people and improve management of staff performance; and
 - iii. Payroll remediation project – to improve efficiency in the processing of the payroll.

¹ International Public Sector Accounting Standards.

18. These projects are progressing satisfactorily and are expected to be completed by the end of 2018.

2018 Budget

19. Under the current arrangements for approving the SPC budget, ARC is tasked to review the budget proposed by management and provide a recommendation to the CRGA Subcommittee on the Implementation of the Pacific Community Strategic Plan.
20. The committee met in December 2017 and provided the subcommittee with its report and recommendations.

Insurance

21. ARC has reviewed the report provided by the insurance broker engaged by SPC to review the Secretariat's insurance coverage and arrangements. As a result of this review, substantial consolidation and harmonisation of insurance cover have been achieved. SPC management is to further review the adequacy and amount of cover appropriate and report back to ARC.

European Union Seven Pillar Assessment

22. ARC has welcomed the outcome of the EU Seven Pillar Assessment, which has found SPC fully compliant with EU requirements. This has positive implications for simplifying the Secretariat's future funding arrangements with the EU. The committee has acknowledged the committed efforts of management and staff to achieve this outcome.

European Union project audits

23. ARC has previously reported to CRGA on the issue of ineligible expenditures associated with the re-auditing of some EU-funded projects. The committee has welcomed management's success in reducing the liabilities resulting from these audits. Negotiations are continuing, but potential further liabilities are likely when additional projects are re-audited. SPC has made significant provisions in the accounts for these liabilities. The potential financial impact on SPC continues to be a concern.

Standing items

24. At each meeting, ARC reviews a number of standing items. These are items which the committee considers important in maintaining oversight of a range of policy and operational issues and areas of potential risk. These standing items are:
- i. audit register – to track progress in implementing decisions of the committee;
 - ii. register of legal actions;
 - iii. register of insurance claims;
 - iv. non-competitive tender register – to monitor compliance with SPC's Procurement Guidelines;
 - v. vendor complaints register;
 - vi. business class travel register – to monitor compliance with SPC Travel Policies;
 - vii. investment portfolio report – to ensure investments are in line with approved policy.

ARC and Internal Audit Charter

25. The existing ARC and Internal Audit Charters were developed following the Independent External Review (IER) in 2012 and subsequently endorsed by CRGA. The committee has agreed that it is timely to review these charters and a number of amendments are now proposed for CRGA's consideration. The proposed charters are attached to this report. The main changes are as follows:

ARC Charter

- i. Authority – that ARC be able to obtain external assistance to perform its duties, without the endorsement of the Secretariat if exceptional circumstances make this appropriate.
- ii. Composition – that the committee comprise a minimum of three independent members and the Director-General. This is an increase in minimum numbers.
- iii. Appointment – to clarify processes for the appointment of committee members.
- iv. Termination – a clause has been added allowing for the termination of a member in cases of fraud or professional misconduct.
- v. Remuneration – to clarify the process for determining remuneration arrangements and levels for committee members.
- vi. Quorum – provisions have been added for a quorum.
- vii. Term of appointments – to limit the term of appointments to two terms of three years. Transitional arrangements are proposed for the current Chair and the other member of the committee who have served since the Committee's charter was revised following the IER in 2012.
- viii. ARC responsibilities – these have been regrouped and re-written for clarity but without any intention to change the meaning.

Internal Audit Charter

- i. Terminology – wording has been updated to reflect changes in terminology.
- ii. The Charter has been amended so that it can apply equally to an outsourced internal audit function (as currently adopted), or one operating in-house (if that is seen as appropriate at some time in the future).

26. ARC supports these amendments to the Charters.

ARC Membership

27. During the reporting period, and in consultation with the Chair, the Director-General approached Caren Rangi, from Cooks Islands, to replace ARC member Savenaca Narube, who withdrew due to other commitments. Ms Rangi is an experienced governance practitioner with many years of sitting on oversight boards in both New Zealand and Cook Islands. Ms Rangi attended the last ARC session to ensure continuity of service and expertise at the ARC.
28. The Committee would like to place on record its appreciation for the cooperation and support it has received from the Director-General, management and staff of SPC over the past 12 months. This has greatly strengthened the effectiveness of the Committee in carrying out its mandate in support of the overall governance responsibilities of CRGA.

Recommendations

29. CRGA is invited to:
- i. note the report from the Chair of the Audit and Risk Committee;
 - ii. approve the proposed amendments to the ARC and Internal Audit Charters;
 - iii. formally endorse the appointment of Ms Caren Rangi as an ARC member, for a term of three years.

Alan Morris
Chair, SPC Audit and Risk Committee



Annex A: Audit and Risk Committee charter; Internal audit charter



Audit and Risk Committee charter

Document version control	1.0
Approved by:	CRGA
Date approved:	

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1. Purpose

The Audit and Risk Committee (ARC) is a sub-committee of the Committee of Representatives of Governments and Administrations (CRGA). ARC assists the CRGA in fulfilling its oversight responsibilities of the financial reporting process, systems of internal control, audit, risk management, effectiveness and efficiency of operations, and compliance with legal and regulatory requirements.

2. Authority

The Audit and Risk Committee (ARC) has the authority to:

- oversee the systems and processes noted above;
- conduct investigations into any matters within its scope of responsibility;
- obtain advice and assistance from outside legal, accounting or other advisers as necessary to perform its duties, in cases where there is suspicion of fraud or gross misconduct;
- report back to CRGA on the work performed by external and internal auditors;
- consult as necessary with SPC's accounting firms in the conduct of its work; and
- seek any information it requires from staff, all of whom are directed to cooperate with the ARC's requests.

3. Composition

The ARC will consist of five members. This will include up to four independent members, including the Chair, appointed by CRGA. The Director-General will be a member of the ARC by virtue of their position.

4. Appointment of members

CRGA will appoint the independent members to the ARC on the joint recommendation of the Chair of the ARC and the Director-General. The ARC Chair and the Director-General may provide the CRGA with a pool of potential committee members to choose from.

CRGA may appoint members out of session.

Members of the ARC will be selected for their individual expertise and appropriate mix of skills.

At least one member of the ARC must possess substantial financial or accounting experience and expertise. Other members must demonstrate expertise in audit, legal, governance, risk and oversight functions.

The initial appointment will be for a maximum period of three years. Members may not serve more than six of years. When appointing members, CRGA will have regard to timing of the appointments to ensure end dates are staggered to ensure continuity.

The chair of the ARC will be appointed by CRGA from one of the independent members and report directly to the chair of CRGA.

The CRGA may terminate an ARC member in cases of fraud or professional misconduct.

5. Remuneration of members

Members, who are not domestic or international public servants, will be paid an honorarium for their participation in meetings. The honorarium will be set at the time of the member's appointment

and will be linked to the United Nation's consultant's remuneration scale. The Chair will be paid at a higher daily rate than other members.

SPC will pay for members travel and per diems for attendance at any face to face meetings.

6. Meetings

The ARC will meet at least three times annually. Additional meetings may be called by the Chair, as needed. All committee members are expected to attend each meeting, in person or via tele- or video-conference.

Meetings may be held virtually through videoconference or teleconference facilities.

If the Chair is unable to attend a meeting, the Chair may nominate another member to be Chair for that meeting. If the Director-General is unable to attend, the Director-General may nominate another member of the SPC Executive to represent them at that meeting.

The Audit and Risk Committee will invite members of the Executive, auditors or others as appropriate to attend meetings and provide pertinent information, as necessary.

SPC will provide the secretariat support to the ARC. Meeting agendas will be prepared and provided in advance to members, along with appropriate briefing materials. Minutes will be prepared.

A member who does not attend two consecutive ARC meetings will be considered to have automatically resigned their position and a new member will be appointed following the procedure outlined at paragraph 4.

7. Quorum

The quorum for a meeting shall be a minimum of three members.

The ARC may make decisions out of session providing a minimum of three members provide their agreement in writing to those decisions.

8. Responsibilities

The ARC has responsibilities in the following key areas:

- review of the financial statements
- oversight of internal controls
- oversight of internal and external audit programmes.

Review of the financial statements

The ARC has a critical role in reviewing SPC's annual financial statements. The ARC must consider whether the statements are complete, consistent with information known to Audit and Risk Committee members, and reflect appropriate accounting principles. This review will occur in collaboration with SPC's management team and external audits. It will take into account the findings of the external audit of the financial statements and consider any significant accounting or reporting issues, and all matters required to be communicated to the ARC under the International Public Sector Accounting Standards.

Oversight of SPC's risk management functions

The ARC will keep under review the effectiveness of the risk management and mitigation processes, and internal control systems.

As part of this function ARC will:

- understand the scope of internal and external auditors' review of internal control over financial reporting, and obtain reports on significant findings and recommendations, together with management's responses
- ensure that risk management issues are adequately addressed
- ensure that timely and appropriate corrective action is taken by management.
- keep under review the system for monitoring compliance with rules, regulations and laws.
- ensure that attention is given to the effectiveness, efficiency and economy of operations.

The ARC may initiate, where necessary, special investigations of policies, procedures and practices. It may also review the effectiveness of systems for monitoring compliance with organisational regulations and policies.

The ARC will receive regular updates from management and the organisation's legal counsel regarding compliance matters.

The ARC may receive complaints or allegations from whistle-blowers of alleged serious misconduct by senior management.

Oversight of internal and external audit programmes

For SPC's internal audit function, the ARC is expected to:

- in collaboration with management and the internal auditors, keep under review the internal audit charter, activities, staffing, and organisational structure of the internal audit function
- review and approve the annual internal audit plan.
- review the findings and recommendations in internal audit reports and any management responses
- review the effectiveness of the internal audit function, ensuring continued independence and its performance
- consult regularly with the internal auditor to discuss matters that the Audit and Risk Committee or internal audit believe should be discussed privately.

For SPC's external audit function, the ARC is expected to:

- review, if necessary, the external auditors' proposed audit scope and approach, including coordination of audit effort with internal audit
- review the performance and effectiveness of external auditors
- review external auditors' management letter and management responses
- consult with external auditors to discuss any matters that the Audit and Risk Committee, external auditors or internal audit function believe should be discussed separately.

In addition, the ARC will provide advice to the CRGA on the appointment of external audits and the terms of those appointments.

9. Reporting

The ARC is expected to provide a mechanism for open communication between internal auditors, external auditors, management and the CRGA chair. As such, ARC will provide an annual report to CRGA setting out:

- the ARC's activities for the reporting period, including:
 - findings from the review of the financial statements
 - pertinent issues arising from the oversight of internal controls
 - any significant outstanding issues from the audit programmes
- confirming that the responsibilities under this Charter have been fulfilled
- any issues arising from carrying out any of its functions
- any recommendations to the CRGA.

The ARC will also review any other reports SPC issues that relate to Audit and Risk Committee responsibilities.

10. Review of the ARC Charter

The ARC will from time to time review this Charter and propose changes to CRGA for its approval.



Internal audit charter

Document version control	1.0
Approved by:	CRGA
Date approved:	

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1. Introduction

This internal audit charter (hereinafter referred to as the IAC) sets out the purpose, authority, responsibilities and general framework of the internal audit function at the Pacific Community (SPC).

The internal audit function is overseen by the Audit and Risk Committee.

2. Role

The internal audit function is an integral part of the SPC's corporate governance framework to add value and improve SPC's operations. It is intended to provide an independent, systematic and objective approach to evaluate and improve the effectiveness of the organisation's internal control, risk management and governance processes.

The internal audit function will assist SPC to achieve its strategic objectives, as articulated in its strategic plan and ensure the effectiveness of the systems and processes that support resource use and programme delivery.

The internal audit function will comprise the following types of services:

- *Assurance services* – An objective examination of evidence for the purpose of providing an independent assessment of governance processes, risk management and internal control.
- *Consulting services* – An advisory service that is intended to add value to and improve the SPC's systems, procedures and operations.
- *Investigative services* – These are conducted based on reports of unusual or suspicious activity. Investigations would usually focus on specific actions or behaviours of a work unit or individual.

3. Scope of work under the internal audit function

The scope of activity of the internal audit will be sufficiently comprehensive to result in the effective review of operations of all SPC's divisions, programmes, sections and teams. It covers SPC's governance, financial, administrative and operational systems and activities.

The areas of focus under the internal audit function include:

- (a) **Financial audit** – reviews internal control processes regarding income and expenditure, cash and other assets, the accuracy of reporting in accordance with established policies and procedures, and complements work done by external auditors.
- (b) **Compliance audit** – evaluates financial and operating controls and their conformance to laws, regulations, standards, contracts, agreements, policies and procedures.
- (c) **Operational or performance audit** – examines the application and use of resources to determine whether they are used in the most efficient and effective ways to meet the SPC's mission and objectives. It could include aspects of a financial or compliance review. Activities such as human resources services, cash handling, procurement, and equipment inventories are generally subject to this type of audit. It aims to promote greater levels of efficiency, effectiveness and economy of operations and enhances continuous improvement and adds value to the organisation's operations.
- (d) **Information system** – reviews the internal control environment of automated information processing systems. These audits typically evaluate a) system input,

processing, and output; b) data controls, backup and recovery plans; and c) systems security.

- (e) **Investigations** – seek to establish impropriety, such as alleged instances of fraud, abuse or waste.

4. Organisation

The head of the internal audit will report to the chair of the Audit and Risk Committee.

5. Authority

The internal auditor and its staff will have full and unrestricted access to all of the SPC's activities, records, premises, staff and information that it considers necessary to undertake its work. All SPC staff are requested to assist the internal audit unit in fulfilling its roles and responsibilities.

The internal auditor will have unrestricted access to the organisation's senior management and the Audit and Risk Committee.

6. Independence and objectivity

The internal audit function will operate independently from the organisation's operations. It will implement its own work plan, which will be determined and approved by the Audit and Risk Committee in collaboration with the Director-General. It determines matters such as audit selection, scope, procedures, frequency, timing or report content that best enables it to fulfill its role.

Internal audit staff do not have direct operational responsibility or authority over any activities audited. They can make recommendations but cannot be involved in implementation or any action that would impair their judgment and independence.

Internal audit staff must exhibit the highest level of professional objectivity in gathering, evaluating and communicating information about the particular activity or process being examined. Their assessments must be objective, based on facts and evidence, and not influenced by other interests.

7. Responsibilities

The scope of internal auditing under this charter encompasses the examination and review of the adequacy and effectiveness of the SPC's governance processes, risk management and internal control processes as agreed on with the Audit and Risk Committee. It also evaluates the quality of performance in the carrying out of assigned responsibilities to achieve SPC's strategic objectives.

The work includes:

- reviewing reliability and integrity of information, systems, processes, policies, procedures and operations, and appraising the adequacy of controls;
- appraising the extent of systems compliance with established policies, procedures and plans, especially where these have a significant impact on operations;
- reviewing controls for safeguarding assets and verifying their existence;
- evaluating the effectiveness, efficiency and economy of resource use;
- evaluating operations or programmes to ensure that results are consistent with established plans, and are implemented as planned;

- monitoring and evaluating governance processes and identifying and reporting significant governance issues;
- monitoring and evaluating the effectiveness of corporate risk management processes and reporting on significant risk exposures and control issues, including fraud risks;
- evaluating specific operations or conducting ad hoc investigations at the request of the Director-General or the Audit and Risk Committee;
- evaluating quality of performance of external auditors and the degree of coordination with the internal audit; and
- recommending improvements to governance, systems, processes, policies and procedures and reducing risk exposure.

8. Reporting and monitoring

Following the conclusion of each audit, a written report will be prepared and issued by the head of the internal auditor for distribution to appropriate parties. The internal audit report may include a response from management on corrective actions taken or to be taken by the management in response to specific findings and recommendations.

The Audit and Risk Committee will follow up on findings and recommendations until they are cleared.

The internal auditor will prepare a regular consolidated report on all activities undertaken in accordance with the approved work plan for presentation to the CRGA Audit and Risk Committee.

9. Professional standards

All internal audit assignments must be undertaken with due professional care. In line with standards of professional internal auditing practice, the internal auditor will ensure that:

- skills, competence, experience and qualifications are appropriate for the audits being performed;
- all internal audit assignments are properly supervised and, where required, on-the-job training provided;
- there is compliance with all relevant standards and codes of ethics; and
- all audit staff undertake continuing professional activities and maintain their affiliation to their professional bodies.

The internal audit work is confidential to the Secretariat and is not to be disclosed to third parties without the authority of the Director-General or Audit and Risk Committee.

10. Audit plan — scope

An annual audit work plan will be prepared and presented to the Audit and Risk Committee for consideration and approval. In formulating the audit plan and annual work programme, the internal auditor will consult with key audit clients, including members of the Executive and heads of programmes and sections. The internal audit plan should be developed using a risk-based methodology.

The audit plan must:

- be sufficiently comprehensive in scope to meet the needs of the Executive and management;
- consider an assessment of risk of audit unit activities, their internal control environment, results of previous audit, and materiality;
- have an appropriate balance between financial, compliance, operational and performance audits. Information systems and special investigations are conducted as required.
- provide a schedule of audits to be undertaken with the resources available during the period covered by the plan; and
- allow flexibility to accommodate special tasks and projects requested by the Director-General or Audit and Risk Committee.

The scope of the internal audit does not extend to the performance of duties normally undertaken by operational units, except as these relate to the performance of audit work.

11. External audit

Internal and external auditors have differing roles and responsibilities. An internal audit is an independent appraisal function that is resident within SPC. The external auditor has the responsibility of expressing an independent opinion of the financial statement and stewardship of the organisation. As there are likely to be overlaps in the work performed by both an internal and external audit, internal audit assignments should be undertaken with the view of maximising the efficiencies of the internal and external audit processes. Internal audit work should not duplicate the work undertaken by external auditors.

12. Amendment of the Charter

Any amendment of the Charter is subject to the approval of CRGA on the recommendation of the Audit and Risk Committee.