

**REPORT OF THE
AUDIT AND FINANCE COMMITTEE
Meeting of the Assembly of Parties
November 6, 2014**

Article 3(8) of the Rules of Procedure of the Audit and Finance Committee (AFC) require that the AFC shall report on its activities and findings to the Standing Committee upon its request or to the Assembly of Parties at its regular meetings and at least once a year. In that context, this report presents a summary of the activities of the AFC during 2014.

The AFC during 2014 comprised of representatives of the Netherlands (Chair), China, Jordan, Kenya and Philippines.

At its March 24, 2014 meeting the AFC agreed upon the following work plan for 2014:

Activity	Scheduled
1. Review of audited 2013 Financial Statements	March 2014
2. Planning for the 2014 External Audit	March 2014
3. Review of IDLO Reserves	March 2014
4. Update on Business Process Review and any developments on internal controls and Enterprise Resource Planning (ERP)	June 2014
5. Update on IDLO's budget recovery and cost allocation policies	June 2014
6. Review of 2015 Management Plan and Budget	September 2014

Summary

The AFC is pleased to see IDLO's budget continue to grow into 2015 and the financial situation continue to remain stable, but looks forward to the organization prioritizing the achievement of its reserve targets as determined during the course of 2014.

2014 has been an important year for IDLO and the AFC, with a number of key positions being filled during the year as the organizational redesign has come towards a close. In addition, a number of management-initiated audits and assessments, summarized below, have been undertaken throughout the year which have created a burning platform for change:

Summary of Audits and Assessments:

- **Annual IDLO Financial Audit and Management Letter prepared by Ernst & Young (EY) Rome, the elected statutory External Auditors of IDLO.** During the annual financial audit work as statutory auditors, EY Rome also performed an analysis of internal controls of IDLO. As a result of this analysis, recommendations regarding procedures, risk assessment and control activities were shared with IDLO. In response, IDLO commented on the recommendations and presented action plans.
- **Assessment of IDLO's operations in Afghanistan performed by Senior Advisor, Jean-Marie Fakhouri.** Based on a site visit to Kabul, observations and recommendations related to human resources and procurement were presented to the Director-General.
- **Afghanistan Procurement Desk Audit performed by Dana-Raluca Albu.** As a result of a review conducted of the procurement process in Afghanistan, key issues and recommendations regarding procedures and procurement structures were presented to IDLO.
- **Internal Control Assessment performed by EY Pakistan.** IDLO assigned EY Pakistan to perform an internal control assessment on the National Justice Sector Strategy (NJSS) program in Afghanistan and to assess Afghanistan's sub-grant process for improvements. Recommendations regarding financial management, sub-granting and procurement were shared with IDLO. IDLO commented on the recommendations and presented actions plans.

The AFC is pleased to note that the recommendations from these audits and assessments, as well as actions from other external audits, have been taken into account by IDLO in the 2015 planning and budgeting process, and will be delivered through the planned multi-year Continuous Improvement Program (CIP), which the AFC endorsed at its meeting of September 25, 2014 (minutes enclosed as Annex 1). The Standing Committee, at its meeting of October 2, 2014 also subsequently endorsed IDLO's CIP.

The AFC 2014 work plan is elaborated below:

1. Review of audited 2013 Financial Statements

The AFC received and reviewed the 2013 audited Financial Statements and Management Letter, and discussed the outcomes of the 2013 audit with EY and IDLO. The AFC welcomed the key recommendation that IDLO move to multi-year funding scenarios to better plan the organization's activities, and in doing that emphasized the importance of scaling up the level of programmatic activities to reduce vulnerabilities. Overall the AFC was pleased to welcome a net positive result of the 2013 audit.

2. Planning for the 2014 External Audit

The AFC provided some feedback to EY as to how their service could be improved, but overall was satisfied with the quality of service provided during the 2013 audit process. At the recommendation of the AFC, the contract with EY to be the external auditor of IDLO has been extended for a limited period of one year to allow for a further assessment of performance to be undertaken. Additionally, the terms of reference for the 2014 audit will be expanded to broaden the scope of audits, and to increase the advisory service provided to IDLO.

The AFC also reviewed a number of other management-initiated audits and assessments conducted by external consultants throughout the course of 2013 and 2014, which have been funded from the vacant Internal Auditor position. The AFC appreciates the steps that IDLO has taken to assess and audit its operations with a view to implementing improvements, and is happy to support IDLO's plan to continue this practice into 2015.

3. Review of IDLO Reserves

In March 2014, the Secretariat provided a paper to the AFC recommending that IDLO adopt an Operating Reserve target of 50% of Annual Operating Costs that would be divided between a short-term Operating Reserve for liquidity fluctuations and a long-term Operating Reserve for emergencies, along with the development of a reserves policy for the Organization.

The AFC recommended to the Standing Committee that the Operating Reserve target be 50% of Annual Operating Costs, plus 25% of Direct Program Costs. The Standing Committee agreed that the proportion of Program Costs kept as reserves could be set at a minimum 12.5%, with a goal of eventually reaching 25%.

4. Update on Business Process Review and any developments on ERP

In 2013, the AFC received an update on the Business Process Review undertaken by Accenture Development Partners (ADP), the outcomes of which were improved processes and procedures for IDLO's Business Development Cycle, and Program Management and Reporting processes.

While the pathway of the Business Process Review and ERP investments originally envisaged during the 2014 process of engaging ADP has not eventuated, the AFC is confident that the appropriately planned and phased review of business processes as part of the multi-year Continuous Improvement Program (part of the 2015 Management Plan) will deliver changes to processes and systems which are fit-for-purpose, and are appropriate for the size and budget of the organization. The AFC foresees that improvements in financial controls and implementation of audit recommendations will come through implementation of CIP initiatives, and looks forward to receiving briefings and updates on this program in the coming years.

5. Review of Cost Allocation and Budget Recovery

In previous years, the AFC has requested a review of IDLO's cost allocation and budget recovery methods, particularly as the Organization aimed to reduce program support cost recovery and to spend more on direct costs to improve quality and in-country efficiency of programs.

IDLO has in place a Time Keeping System that records the time staff spend on direct program implementation, program support, program delivery, and institutional work, which is essential for IDLO's program cost monitoring. The current system of cost allocation is consistent with the AFC's view of how costs ought to be apportioned. However, with further system upgrades and enhanced multi-year budgeting and planning will come improvements to cost allocation mechanisms, which will help IDLO to more accurately cost and manage the costs of its work.

The AFC is confident that a multi-year output-based planning and budgeting process, and ICT systems upgrades, which will be undertaken as part of IDLO's multi-year CIP will greatly assist IDLO in mapping and managing the costs of program implementation.

6. Review of proposed Management Plan and Budget for 2015

The AFC received a presentation of both the 2015 Management Plan and Budget, including the multi-year CIP. The AFC recommended the Standing Committee to approve the proposed budget.

As part of the CIP, the AFC is anticipating increased transparency and accountability in budgeting during the next cycle as IDLO prioritizes the development of a multi-year output-based planning and budgeting process, building on the current output-based process used by IDLO's programs.

ANNEX 1

PROCEEDINGS Meeting of the Audit and Finance Committee September 25, 2014

1. The meeting of the Audit and Finance Committee (AFC) of the International Development Law Organization (IDLO) was held at the IDLO headquarters in Rome.
2. The full list of attendees is attached (Annex A).

AGENDA ITEM 1: Adoption of the agenda (AFC/2014/3.1)

3. The AFC adopted the agenda (AFC/2014/3.1).

AGENDA ITEM 2: Approval of the minutes of the previous meeting of the Audit and Finance Committee meeting of July 16, 2014 (AFC/2014/3.2)

4. The minutes of the AFC meeting of July 16, 2014, were adopted.

AGENDA ITEM 3: Review of IDLO Proposed Management Plan and Budget for 2015 (AFC/2014/3.3)

5. The Secretariat provided a brief presentation of the 2015 Management Plan and the two-year Continuous Improvement Program which will deliver a number of audit recommendations and improved budgeting and accounting systems (Annex B).
6. The Chair requested that the Secretariat provide a presentation to the AFC, when appropriate, outlining the benefits of moving from our current budgeting systems to an output-based planning and budgeting system, and the accounting gaps that would be resolved in moving to an accrual budgeting system which aligns with IPSAS requirements. The Chair gladly noted the inclusion in the 2015 Management Plan of CSI 1, and that IDLO continues to prioritize balancing the program portfolio given its work in fragile states.
7. The Representative of Jordan enquired as to whether the focus on institutional improvements via the Continuous Improvement Program would constitute a shift in the overall composition of the budget and reduction in funding for programs.
8. The Secretariat explained that the ultimate aim of institutional improvements is to build a fit-for-purpose institution that is focused on program delivery. IDLO has benefited from the generous multi-year contribution in unrestricted funding from the Government of the Netherlands in recent years, which has enabled the organization to build up human resources for institution-building. The Chair endorsed the value of prioritizing institutional improvements.

9. As requested by the Chair, the Secretariat provided an overview of the new role of the Chief Operating Officer, outlining the critical role of bringing together Human Resources, Finance, Procurement, ICT and Office Services functions to break down silos and work across functions. The positions of the respective Heads of Service (for instance Head of Finance, Head of Human Resources) remain in place to ensure adequate oversight and management of each functional area.
10. The Representative of the Philippines enquired as to whether the move to output-based planning and budgeting is envisaged to be accompanied by the development of performance indicators and metrics and end-to-end process management. The Secretariat confirmed that the development of metrics and performance indicators is a critical aspect of moving to output based planning, and in analyzing and reviewing internal business process. Performance reporting, for IDLO's programs and institutional efficiency and effectiveness, will be an aspect of the two-year Continuous Improvement Program.
11. The Secretariat presented the Proposed 2015 Budget, showing a total revenue estimate for 2015 of 35.2 million euro and a total expenditure estimate of 34.7 million euro resulting in an overall surplus of 0.5 million euro.
12. The Chair provided an overview of how expenditure is allocated in the current budget, defining the following concepts:
 - Direct program costs – which includes staff time on program work, travel, and supporting materials;
 - Program support costs – which includes program development, financial monitoring, purchase, logistics and human resources management;
 - Program delivery costs – which includes the time spent by staff members in the benefit of the program, development manuals and training courses;
 - Institutional costs – which include general management, financial management, donor, government and public relations, and knowledge development.

In addition, the Chair outlined that improvements to budgeting and cost allocation would come naturally as part of the move to output-based planning and budgeting.

13. The AFC agreed to recommend to the Standing Committee that the Proposed 2015 Budget be approved, with the expectation that the 2016 budget would be an output-based budget.
14. The AFC agreed to endorse the Continuous Improvement Program as part of the 2015 Management Plan, which will deliver on key systems improvements of importance to the AFC and responses to audit recommendations.

AGENDA ITEM 4: 2014 Report of the Audit and Finance Committee to the Assembly of Parties

15. The Chair proposed to prepare a draft report, including a summary of 2014 initiatives, which would be circulated to the AFC Members before being provided to the Assembly of Parties.

AGENDA ITEM 5: AFC Proposed Work Plan for 2015

16. The Representative of Jordan enquired as to whether the Audit and Finance Committee would be required to consider audit recommendations and follow-up actions as part of the Work Plan.
17. The Chair proposed that the AFC monitor the progress of aspects of the Continuous Improvement Program, with the expectation that implementation of the Continuous Improvement Program will address audit recommendations in a more structured and cohesive manner.
18. The AFC adopted the Work Plan for 2015 (Annex C) which includes review of the quarterly financial updates provided to the Standing Committee.

AGENDA ITEM 6: Other Business

19. The Chair updated members of the AFC on the final Assessment of IDLO undertaken by Ernst & Young on behalf of SIDA. The Chair informed members of an updated statement written as AFC Chair which is intended to be conveyed to SIDA, at the appropriate time. The statement confirms the confidence of the Chair of AFC in the present quality of the internal management and control systems of IDLO, and endorses the organization's need for unrestricted funding to strengthen of the organization for the long term impact of IDLO's program activities and to assure the release of the conditional part of the Dutch funding.
20. The Chair thanked all participants, noting in particular the trust and confidence in the Management Team of IDLO and the positive change that will come with the Continuous Improvement Program, and closed the meeting.

Annex A

LIST OF ATTENDEES

Meeting of the Audit and Finance Committee

September 25, 2014

Members of the Audit and Finance Committee

The Netherlands (Chair)

1. Mr. Lex van der Hoeven, Controller, Stabilization and Humanitarian Aid Department, Dutch Ministry of Foreign Affairs

Kenya

2. Mr. Charles Ooko Otieno, Second Secretary, Embassy of Kenya

Jordan

3. Mrs. Reima Dubayah, Attaché, Embassy of Jordan

The Philippines

4. Mr. Enrique V. Pingol, First Secretary and Vice Counsel, Embassy of the Philippines

IDLO

5. Ms. Mira Bacelj, Chief Operating Officer
6. Mr. Albert Mola, Head of Finance
7. Ms. Karine Charmel
8. Ms. Morgan Barr

Annex B

Summary Report to AFC

IDLO's 2 year Continuous Improvement Plan

Based on the Strategic Plan 2013-16 and following the implementation of IDLO's new organizational design during 2013-2014, the priority in 2015 will be to continue to strengthen its institutional and workforce effectiveness and efficiency through the launch of a two-year program of Continuous Improvement to its services. The **two-year Continuous Improvement Program (CIP)** will focus on the implementation of concrete outputs and will deliver:

- increased quality and efficiency of IDLO's corporate services;
- strengthened management of people, budgeting, finances, procurement, infrastructure and ICT;
- enhanced service delivery to the field; and
- an engaged, equipped and empowered workforce.

The CIP will focus on implementation and be evidence-based, including benchmarking with comparable organizations which will ensure that IDLO will continue to implement best practices to enhance accountability and transparency to its Members and donors. The CIP will also provide the framework for enabling the organization to respond to the various audit recommendations, emanating from External Auditors and recent organizational assessments.

The CIP will contribute to the achievement of the Institutional Reforms set out in IDLO's Strategic Plan 2013-2016, as well as the 2015 Management Plan's Critical Strategic Initiatives (CSIs), namely CSIs 5 and 6 below:



Critical Strategic Initiative 5 (CSI 5): Improve efficiency, effectiveness and accountability

With increased support, funding and greater visibility comes greater scrutiny. IDLO is committed to improving its efficiency and effectiveness while at the same time strengthening its accountability to Members, donors, partners and other stakeholders, including its beneficiaries – the communities and individuals whose lives its programs seeks to improve through development in the rule of law. It will do so by focusing on the following CIP initiatives in 2015:

A. Organizational wide outputs-based planning, budgeting and reporting

To foster increased transparency and strengthened accountability IDLO will develop and pilot its first output based planning, budgeting and reporting system. This *performance-based framework* will ensure that all IDLO outputs are costed, and have key performance indicators (KPIs) specified in terms of quantity, quality and timeliness targets. As previously reported to the Standing Committee, Organization-wide KPIs will be established and tracked on a regular basis. This will bring IDLO into line with other organizations, including IGOs such as the Organization for Economic Co-operation and Development (OECD) that is leading work in this area.

This output-based budgeting approach will put in place the essential building blocks to enable IDLO to move to a *multi-year budgeting and funding* basis, *accrual budgeting* and an output based *cost allocation* system. The latter will enable better control for IDLO in attributing costs to program implementation versus institutional activities.

Output-based Planning and Budgeting will also set the vision and framework for IDLO to move forward with strengthened financial performance reporting, implementation of a monitoring system for the management of sub-grants and implementation of *International Public Sector Accounting Standards (IPSAS)*. This framework also provide IDLO with the technical requirements for upgrading its existing ERP, along with the work being done on business process redesign.

Building on the work undertaken in 2014, IDLO will introduce a Risk Management Framework in 2015, with the implementation of a risk register that will monitor and mitigate risks, and be updated on a quarterly basis. In managing its risks, IDLO will also ensure prompt responses to audit recommendations that will foster confidence and trust in the Organization's management and leadership.

B. Enhanced service delivery via improved business processes

Following a preliminary review that started in 2014, IDLO's end-to-end business processes will be improved to ensure that services are *client-oriented, efficient and effective*. Simplified,

integrated and efficient processes will be implemented in the areas of financial services, human resources, procurement, office services and ICT services to ensure that all program and field operations are optimally serviced.

User-friendly guidelines and tools will be developed to support program and field employees in their day to day operations.

C. Upgrade of information and communication systems

New and improved business processes will need to be enabled by efficient communications and technology solutions. An ICT needs assessment will be undertaken as part of the implementation of the improved business processes. Modernized and value for money ICT systems will be implemented over the next two years across all IDLO offices.

Critical Strategic Initiative 6 (CSI 6): Invest in People

D. Review staff rules including contractual model and scheme for recruitment and engagement of talent across all IDLO locations

Following the adoption of revised Staff Regulations by the Assembly of Parties in 2013, the Organization embarked on a review of the Staff Rules in 2014. It is imperative that the Staff Rules are strongly supported by an employment policy framework appropriate for IDLO. Therefore, the next step in 2015 will be for IDLO to undertake an evidence-based independent assessment of contracting schemes for recruitment and engagement of talent across all IDLO locations. The need for this independent assessment is consistent with recent audit recommendations that request IDLO to define salary levels of all international and local employees, in accordance with the economic conditions of the countries in which they operate.

E. Strengthened leadership and people management

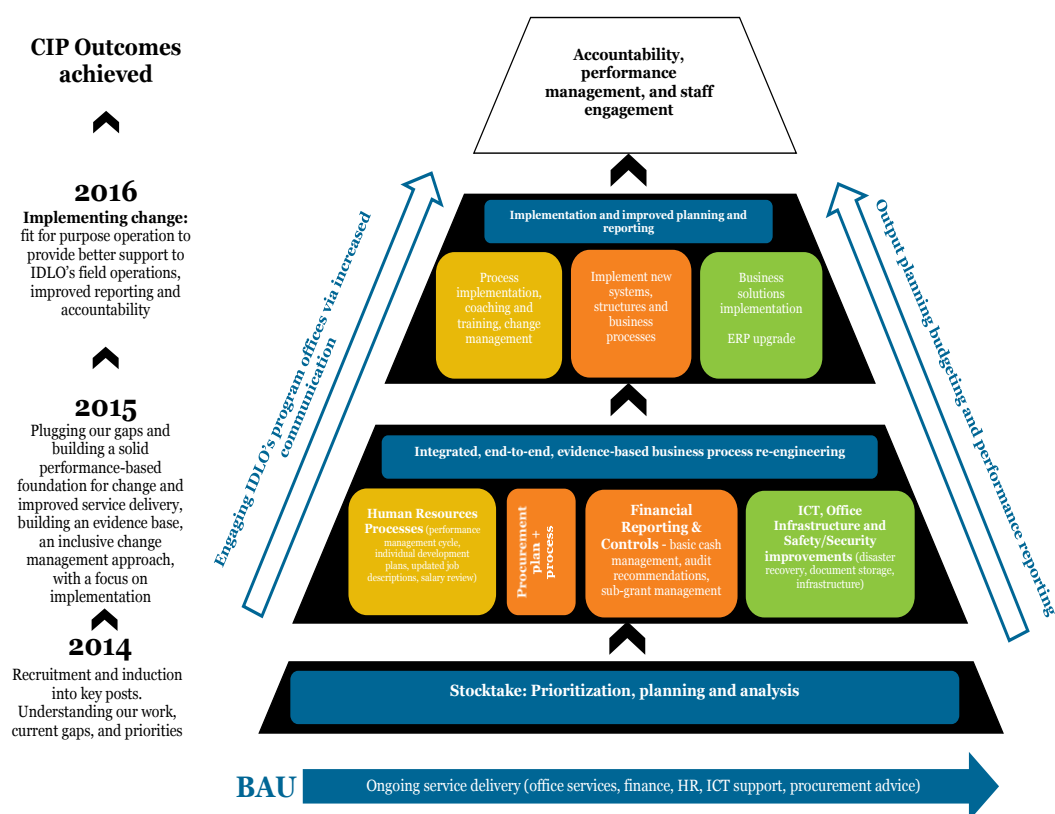
Leadership and People Management are essential to good governance and employee engagement. An updated performance management cycle for all employees will be introduced in 2015 as part of the CIP. It will be complemented with leadership and management training for all IDLO managers across all locations.

Furthermore, in 2015 all managers will need to ensure that job descriptions are updated for their team members, as well as ensuring that an individual development plan has been actioned and discussed with their employees. Increased implementation of learning and training activities for employees is planned as a priority in 2015.

F. Strengthen internal communications across departments, offices and between field and headquarters

Strengthened internal communications and higher employee engagement will be a key thread throughout the Continuous Improvement Program. The program will be led and managed in an inclusive way, involving IDLO employees from across all offices. Increasing collaboration laterally and breaking down silos between departments, as well as improved people management and strengthened leadership will result in a more linked-up and ‘team’-oriented organization.

Chart 1: 2 year - Continuous Improvement Program – high-level vision and timeframe



Annex C

AFC 2015 PROPOSED WORK PLAN FOR QUARTERLY AFC MEETINGS

March 2015 Meeting

- **Review 1st Quarter 2015 Financial Update**
- Review 2014 Audited Financial Statements and Management Recommendation Letter (External Auditors will be present)
- 2015 External Audit planning
- Review Progress and Plans on IDLO's Continuous Improvement Plan 2015-2016
 - *(specific reform items/audit actions plans would be covered)*

June 2015 Meeting

- **Review 2nd Quarter 2015 Financial Update**
- Review Progress and Plans on IDLO's Continuous Improvement Plan 2015-2016
 - *(specific reform items/audit actions plans would be covered)*

September 2015 Meeting

- **Review 3rd Quarter 2015 Financial Update**
- Review IDLO's 2016 Management Plan and Budget
- Review Progress and Plans on IDLO's Continuous Improvement Plan 2015-2016
 - *(specific reform items/audit actions plans would be covered)*