

CHAPTER 1

COMMENTS RELATING TO THE GENERAL SECRETARIAT



This chapter addresses issues, concerns, and recommendations that the Board wishes to bring to the attention of the General Assembly, Permanent Council, and Secretary General regarding the Organization of American States' (OAS) General Secretariat. It includes a summary of the financial condition of the Regular Fund and Specific Funds, and also addresses management initiatives undertaken to implement recommendations contained in last year's Board Report as well as new issues identified by the Board.

Status of Recommendations from the Board's 2004 Report

In its 2004 Report, the Board discussed several issues related to the operation of OAS and provided specific recommendations to address them. The Board is satisfied with the progress made by OAS' General Secretariat (GS/OAS) in implementing its recommendations despite OAS' limited resources. The Board is closing seven recommendations that it made in its 2004 report. Twelve recommendations made in the 2004 report remain open, although the Board has revised some of these to accommodate changing circumstances. Information on these recommendations and new issues are described in detail in the following sections.

Financial Statement Audit Reports

The independent external auditing firm, SB & Company, LLC (SBC), conducted the audits of the 2005 financial statements of the

significant funds and entities managed by OAS' General Secretariat and issued unqualified ("clean") opinions, the highest level audit results, on all of the funds and entities it audited. The financial statement audits were designed to focus on appropriate key areas based on SBC's assessment of risk.

Ernst & Young, LLP, was performing the audit of OAS' Retirement and Pension Fund financial statements. This had not been completed at the time of the Board's report. This is the second consecutive year that the Board did not receive information from the Retirement and Pension Fund for review in advance of the Board meeting. The Board did review draft unaudited financial statements and met with the Director and the Treasurer of the Retirement and Pension Fund. As a result of this limited assessment, no areas of significant concern came to the attention of the Board.

Internal Control Environment – Independent Auditors' Management Letter

Overall, SBC reported that OAS' internal control environment was effective. There were no material weaknesses or reportable conditions in the audit reports. However, SBC did note a number of internal control issues and recommendations for improvements that it reported to appropriate officials in GS/OAS.

Financial Condition of the OAS Regular Fund and Specific Funds

The major objective of the Regular Fund, financed principally by quotas from Member states, is to provide general services required by the General Secretariat, as well as technical supervision and administrative support to the General Assembly, Permanent Council, Inter-American Commission of Human Rights, Inter-American Commission of Women, Inter-American Juridical Committee, Inter-American Children's Institute, Inter-American Court of Human Rights, Inter-American Commission for Drug Abuse Control, and Inter-American Communications Commission.

The Regular Fund's fund balance was \$10.2 million as of December 31, 2005, which was an increase over the December 31, 2004, fund balance of \$7.6 million. This increase was mainly due to an increase in quota collections and rentals, and a decrease in personnel and administrative costs.

Quota collections during 2005 totaled approximately \$76.3 million compared to \$67.1 million in 2004. The balance of quotas in arrears decreased to \$18.6 million as of December 31, 2005, compared to \$21.2 million as of December 31, 2004. The number of Member states with quotas in arrears decreased from 16 countries in 2004 to 12 countries at the end of 2005.

During 2005, the total expenditures and obligations of \$77.2 million was \$1.3 million less than the adjusted 2005 budget of \$78.5 million. In 2004, the total expenditures and obligations of \$79.9 million exceeded the 2004 adjusted budget of \$79.6 million by approximately \$250,000.

Regular Fund

The following tables show the Regular Fund Financial results from 2001 to 2005.

Changes to the Regular Fund (In millions)

Year	2005	2004	2003	2002	2001
Income (A)	\$ 79.8	\$ 68.3	\$ 71.9	\$ 98.1	\$ 90
Expenditures	77.2	79.9	76.3	76.3	76
Operating Results Increase (Decrease)	2.6	(11.5)	(4.4)	21.8	14
Fund Balance	\$ 10.2	\$ 7.6	\$ 19.1 (B)	\$ 44.5	\$ 22.7

Notes:

- A) Income includes quotas collections, other income from support to FEMCIDI projects, and interest income.
- B) The \$19.1 million fund balance in 2003 is net of \$21 million in supplementary appropriations transferred in January 2003 to the specific funds due to General Assembly resolution 831.

The following table shows Regular Fund quota collections from 2001 to 2005.

Regular Fund Quota Collections (In millions)

Year	2005	2004	2003	2002	2001
Beginning balance of quotas from prior years	\$ 21.2	\$ 14.6	\$ 10.6	\$ 31.5	\$ 43.4
Current year quotas	73.7	73.7	73.7	73.7	73.7
Quota collections	(76.3)	(67.1)	(69.7)	(94.6)	(85.6)
Quotas in arrears at year-end (C, D)	\$18.6	\$ 21.2	\$ 14.6	\$ 10.6	\$ 31.5

Notes:

- C) Balances exclude quotas in arrears from Cuba, which were \$2.2 million.
- D) Countries with largest quotas in arrears include: Argentina, \$10.8 million (58 percent of quotas in arrears), Brazil, \$3.4 million (18 percent) and Venezuela, \$2.4 million (13 percent).

Specific Funds

The Specific Funds are financed by grants or bequests for activities specified by donors, and any other contributions by national or international public or private entities for carrying out activities or programs of the General Secretariat. These funds also include designated funds that have been segregated for a specific purpose and whose use is restricted through designation by the General Assembly or the General Secretariat.

In 2005, contributions to the Specific Funds decreased by 34 percent from the amount contributed in 2004. Specific Funds financial results from 2001 to 2005 are included in the following table.

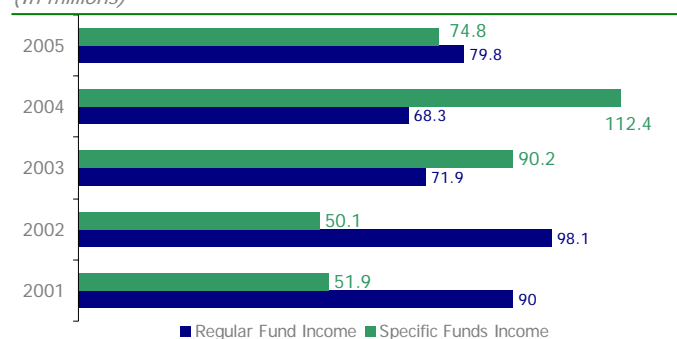
Specific Funds financial results

(In millions)

Year	2005	2004	2003	2002	2001
Income	\$74.8	\$ 112.4	\$90.2	\$50.1	\$51.9
Expenses	82.6	91.3	74.7	58.6	43.3
Net Income (Expense)	(7.8)	21.1	15.5	(8.5)	8.9
Fund Balance	\$51.8	\$ 59.6	38.5	\$23.0	\$31.5

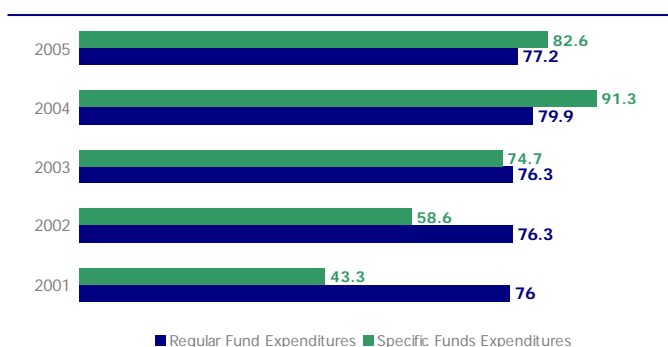
Comparison of Regular Fund and Specific Funds Income

(In millions)



Execution of the Regular Fund Compared to the Specific Funds

(In millions)



- Regular Fund execution has remained constant
- Specific Funds execution has increased 91% since 2001
- Specific Funds execution now represents 52% of transactions versus 36% in 2001

2005 BOARD OF EXTERNAL AUDITORS RECOMMENDATIONS

Quota Collections

Although quota collections did improve slightly in 2005, it is still an issue that impacts OAS' overall financial condition. OAS has implemented an incentive that would decrease quotas by two percent if paid by a certain date. Recently, there have been discussions within the governing bodies of OAS about instituting penalties for countries that do not pay quotas in a timely manner; however, no agreements were reached on this issue.

Currently, Member states establish their own payment plans for their quotas. In many cases, the Member states provide their quota payments late in the year. This often creates a difficult cash flow situation within GS/OAS because the timing of the quota payments is irregular when compared to the budget execution. OAS sometimes has a difficult time meeting payroll and other fixed costs. Capital and project planning can be difficult, because GS/OAS does not always know when or if funds will be available. OAS might want to consider changing the quota requirements so that Member states would pay their quotas in advance or at set intervals, so that the operating budget would be consistent.

Immediate measures are necessary to increase quota collections. The Board supports the efforts of the Secretary General and the Assistant Secretary for Management to bring this matter to the attention of the Member states in order to obtain the resources required to meet OAS' mandates without incurring future operational deficits. However, more needs to be done to ensure that OAS has the funds it needs to carry out its functions.

1.1 The Board recommends that the Permanent Council assign a high priority to the payment of quotas in arrears and identify effective methods

to promote timely payments that reduce the level of quotas in arrears.

1.2 The Board recommends that the Permanent Council consider changing the quota requirements to have Member states fund their quotas by an earlier date.

Budgetary Resources

Even if quotas were collected in a timely manner, the financial condition of the Regular Fund would still be an issue since the annual quotas do not cover the operating budget of the GS/OAS. With annual quotas fixed at \$73.7 million for the past several years, OAS has undergone a continuing decline in the amount of inflation-adjusted cash resources. For the past few years, the Regular Fund budgets have remained flat or declined despite the requirement to finance salary increases set by United Nations rules and absorb inflationary cost increases.

As discussed above, the financial condition of the Regular Fund did improve slightly in 2005. In addition, OAS informed the Board that during a special session in January 2006, the General Assembly adopted a tentative measure to increase the annual quota to \$76.2 million for 2007. The CAAP has recognized the difficult financial position of GS/OAS, and has initially approved a \$5.2 million increase for the 2006 budget. Although the General Assembly has increased the annual quota, this increase would not fund the budget ceiling for 2007 of \$81.5 million.

During 2005, OAS underwent a major reorganization which it believed would improve the budgetary situation of the organization. It developed a new Office of Planning, Control, and Evaluations to work on budgetary issues, such as developing strategic goals. At the time of the Board's meeting, little progress had been made in this area. The Board believes it is essential for OAS to take a hard look at its priorities and determine opportunities for cost savings.

The Board understands that OAS has already made numerous cuts in staffing and other services. In some cases, as discussed below, the Board is concerned that the cuts may have harmed the internal control environment. It is essential for OAS to develop a well-thought out and supportable plan for budgetary improvements. The budget constraints of OAS must be adequately addressed in order for OAS to continue to meet its goals and mission.

In addition to considering additional budgetary reductions, OAS needs to be proactive in searching out innovative ways to increase revenues. For instance, OAS may not be maximizing the potential of a piece of property that is currently used by IADB (located at 16th Street and Euclid Street in Washington D.C.). Also, there may be some potential for increasing rental income in its General Secretariat Building.

1.3 The Board reaffirms its recommendation that the Permanent Council revisit the quota cap to ensure consistency between the mechanism of setting OAS quotas and the mechanism of setting expenditures, such as personnel costs. At a minimum, the Board recommends that an automatic process to increase annual quotas to fund inflationary cost increases for salaries should be instituted.

1.4 The Board reaffirms its recommendation that the Permanent Council implement a planning process that identifies strategic objectives and priorities, allocates scarce budgetary resources to achieve OAS' key goals, helps to generate reliable cost estimates of mandates before their approval, and supports accountability for results.

1.5 The Board reaffirms its recommendation that GS/OAS establish a visible and systematic budget savings initiative that augments the

efficiency of OAS operations and improves asset management.

1.6 The Board recommends that GS/OAS consider other sources of income that are available, including making a decision on how to maximize the potential of its property located at 16th Street and Euclid Street in Washington D.C.

Recovery of Administrative and Oversight Costs

OAS has a requirement that two percent of all new Specific Fund contributions be used to fund administrative support and other overhead expenses. The Board found that OAS often waives this requirement if the contributor specifically states that they do not want the Specific Funds used for overhead.

Although the Board understands the intent behind this type of request, the Board does not believe that the implications are being adequately conveyed to the contributors. As the number of Specific Funds increases, so does the support costs. Without a portion of the contributions going toward recovery of administrative and oversight costs, the Regular Fund, which is already in a difficult financial position, will be strained even more.

The Board is also concerned that the two percent allocation for overhead is not based on a cost analysis. OAS needs to establish an enforceable, supportable, and consistent mechanism for recovering administrative and oversight costs. However, the Board does not believe it is appropriate to institute a uniform, across-the-board fee for each project. Donors should be able to clearly see the benefits they are receiving from providing funds to cover administrative and oversight costs. Some projects might require more administrative support or oversight than other projects. Therefore, OAS needs to tailor a cost estimate for each proposed donation to clearly understand the cost implications for OAS and to be able to quantify an appropriate fee to

charge for these funds. If a donor is unwilling to allow its funds to be used to cover the administrative and oversight charges, OAS management will need to determine whether the funds should be accepted. Having the cost information available will make an informed decision easier to reach.

OAS has established a new office, called the Office of Planning, Control, and Evaluations. One of the missions of this new Office is to work with the Secretary General to develop a new policy on overhead.

1.7 The Board recommends that GS/OAS perform an overhead cost analysis that identifies all administrative and oversight costs used to support Specific Fund donations. This information should be used to estimate the costs associated with each proposed donation to a Specific Fund.

1.8 The Board encourages GS/OAS to develop an enforceable and consistent mechanism for calculating overhead to Specific Funds. The Board also encourages management to work with donors to help them understand the benefits they would receive from funding the administrative and oversight costs. OAS needs to assess any proposed donations that will not fund these costs to determine whether the funds should be accepted.

Reporting Financial and Budgetary Results

OAS' financial statements provide an audited confirmation of how management used and allocated all of OAS' financial resources among different entities and related funds. GS/OAS made improvements in the preparation of the 2005 financial statements. Most of the financial statements were completed earlier than in former years. The Board congratulates GS/OAS for these improvements. However, the Board believes that some additional improvements could

make the financial reporting more useful, timely, and transparent to users.

For instance, the Board believes that OAS' statements could be enhanced by linking the actual use of financial resources to the achievement of specific strategic objectives and priorities. OAS has recently created a new Office of Planning, Control, and Evaluations. One of the areas this Office is planning to focus its efforts is developing a results-oriented budget. Once this is done, the financial statements could be organized in a similar manner. Although the Board believes this might take several years to implement, it would be a useful tool. For this project to be successful, the Board believes that high-level management will need to support the initiative. In addition, GS/OAS will need to get the support of other interested parties.

1.9 The Board recommends that GS/OAS financial reports should provide, to the extent possible, a link between the use of resources and achievement of strategic goals and objectives in a manner that is most useful to Member states, management, and donors. GS/OAS should work with all interested parties before implementing the new financial statements, to ensure that they are comfortable with the new format and information being included.

The Board also believes that OAS's Regular Fund financial statements could be improved by including a Statement of Cash Flow. A cash flow statement shows incoming and outgoing money during a particular period. As an analytical tool the Statement of Cash Flow is useful in determining the availability of funds to cover expenses and would highlight the financial condition of the Regular Fund.

1.10 The Board reaffirms the recommendation that GS/OAS include a Statement of Cash Flow in the audited yearly financial statements of the Regular Fund.

Reorganization

The Board was pleased with OAS' efforts to achieve efficiencies and economies through the 2005 reorganization. It is natural, during a reorganization to see some uncertainty related to roles and responsibilities, issues related to lines of communication or authority, and certain other types of disorganization. During this time of change, the Board would like to encourage OAS management to make conscious efforts to keep lines of communication open and to address organizational issues promptly. The Board did note that policies and procedures and job descriptions related to some of the new organizations had not yet been updated.

1.11 The Board recommends that GS/OAS develop appropriate policies and procedures and job descriptions for all of the new sections created by the reorganization.

Training

Human capital is one of OAS' most significant assets even though it is not recorded in the financial statements. OAS deserves to have a continuing and adequate training program to maintain and upgrade skills of OAS' employees.

As noted above, the quota cap for the past several years imposed the requirement to implement spending reductions throughout OAS. These decreases have led to personnel reductions and have inhibited progress in ensuring sufficient training for OAS staff. The Board feels that professional development is important in any organization; however, in light of the limited staff in many key sections of OAS, adequate training becomes even more essential. This should include cross-training of individuals to ensure that there is adequate coverage of all key functions. The Board continues to support the efforts of Human Resources Services to develop a professional development strategy.

1.12 The Board reaffirms its recommendation to reexamine the training budget. Given the decrease observed in recent years, the Board

encourages GS/OAS to find cost-effective alternative methods to train staff. These methods could include internal instructors, training agreements with appropriate institutions, and self-paced computer training methods. This training should be developed with the input of the Office of the Inspector General ("OIG") to ensure that enhanced training and awareness of key internal controls are covered. In addition, the Board encourages OAS to require all employees performing technical work, in particular accounting and finance functions, to complete annually a minimum number of training hours. This should include cross-training to ensure that all key functions have adequate coverage.

National Offices

The external financial statement auditor, OIG, and OAS management have identified concerns with the control environment at the National Offices. The Board believes that OAS is working to coordinate and reassess the role of the National Offices to ensure they are meeting OAS' intended goals. It will review the results of this effort during the next Board meeting.

However, OAS needs to consider the internal controls in place at the National Offices to ensure that they are appropriate for the current level of staffing. The external auditors reported instances where employees were unclear about the requirements to process disbursements and concerns that the limited staffing in the National Offices (a Director, administrative assistant, and driver/messenger) could lead to inadequate segregation of duties. The OIG also expressed concern that not all of the National Offices were linked to the OASES system.

The staff in the National Offices needs to be adequately trained and monitored. Although OIG tries to audit all of the National Offices on a cyclical basis, its budget is limited and

so it is not able to perform as many of these audits as it once did. OAS may want to consider having experienced staff make short site visits to the National Offices on a regular basis to ensure that policies and procedures are complied with.

1.13 The Board recommends that the GS/OAS ensure that staff at the National Offices are adequately trained and that an appropriate methodology to monitor internal controls at the National Offices is established.

Control Environment

Fellowships

The Board was informed about some serious internal control issues related to Fellowships in 2005. At one point, OAS believed that approximately \$2 million had been spent over what had been budgeted for Fellowships. Funds to cover these additional expenditures had to be borrowed from the Capital Fund. Ultimately, over \$500,000 was deobligated, and GS/OAS was able to use Reserve Funds to reimburse the Capital Fund for the amount borrowed.

OAS reported that this situation occurred principally for two reasons. Fellowships were approved outside of the normal process. A new Director has been put in charge of this area, who informed the Board that no Fellowships will be approved outside of the normal process.

Another reason for the budgetary issues was that the Fellowship managers did not always know the resources available. The new Director indicated that no scholarships will be approved until there is clear information on resources available for Fellowships.

The external financial statement auditors also reported that Fellowship staff was not adequately reviewing the contractor's invoices to ensure proper fees were being paid. The external financial statement auditors reported that the invoices received from the Fellowship contractor did not

include enough detail for OAS to ensure that proper fees were charged. OAS submits a general purchase order for the contractor with an estimate of general expenses in order to obligate funds.

In addition, the Board believes that attention should be given to the length and cost of a study program before a scholarship is established to determine the appropriateness of a particular educational institution and, subsequent thereto, to determine future liabilities.

1.14 The Board recommends that GS/OAS ensure that the internal policies and procedures related to Fellowships are appropriate. In addition, GS/OAS should develop and implement a process to ensure that all internal policies related to Fellowship selection and approval are adhered to and adequately documented.

1.15 The Board recommends that GS/OAS work with the external contractor to modify the contract to clarify each party's roles and responsibilities. GS/OAS should appropriately monitor the external contractor to verify that payments are accurate and made for approved students. GS/OAS should also revise the purchase order process to provide identification of the students approved for fellowships and an estimate of the fellowship cost and administrative fees for each year committed to the student.

Disbursements

Both the external financial statement auditors and the IG noted issues related to disbursements.

There is a formal vendor listing in the OASES system. In order for a requisition to be processed, the vendor name must already be in the vendor listing. However, the Board determined that there was no formal process to ascertain

that new or existing vendors were valid. There was also no formal process to remove vendors no longer needed from the system.

The external financial statement auditors and the IG also reported concerns with the use of “generic vendors” on purchase orders. OAS’ internal policies allow staff, in rare circumstances, to prepare a purchase order without listing the specific vendor that would be used. However, this has become a common practice in National Offices.

OAS’ management has indicated that it has made progress in both of these areas, but has not completed its efforts. Each of these issues increases the risk that unauthorized disbursements and misappropriations of cash would not be identified and prevented.

1.16 The Board recommends that GS/OAS improve controls over approved vendor listings. This should include developing a formal process to ascertain that new and existing vendors are valid.

1.17 The Board recommends that GS/OAS work to eliminate the use of generic purchase orders without advance approval. This approval should only be given in exceptional circumstances.

Information Technology System

OAS has improved controls over people that have “super user” access in the OASES system. However, nine people within the administrative areas still have this type of access. The Board is concerned about this situation. OIG is currently performing an assessment of the OASES system, including the use of super users. The Board is not making a recommendation on this issue in its report. However, the Board believes that OAS should promptly consider any findings or recommendation made by OIG in its assessment.

OAS management informed the Board that they have developed a contingency plan for the computer systems. However, due to budget limitations this plan has not been implemented or tested.

1.18 The Board recommends that GS/OAS ensure that an appropriate contingency plan is implemented and tested.

Contractor Oversight Process

OAS has improved the oversight of the contractor process, but management agrees that there is still room for improvement. For instance, OAS has added a step to ensure that all requests for contractors comply with internal policies and procedures. However, they have not completed automating the process for requesting contractors. The Board is concerned that many offices within OAS rely on contractors to perform regular, day-to-day operations. This is a long-standing issue because the staffing levels are not adequate to complete mandates. However, the intent of the contracting process was not to supplement limited staffing, but instead, to use the funds for limited projects or for specialized technical skills.

1.19 The Board reaffirms its recommendation that GS/OAS continue to strengthen the CPR oversight process and ensure compliance with the Performance Control Rules.

Monitor Compliance With Debt Covenants

During the audit of OAS’ 2004 financial statements, the external auditors noted that there were instances of noncompliance with various debt covenant requirements. Although OAS has improved compliance with these debt covenants, it is still not in complete compliance.

1.20 The Board reaffirms its recommendation that GS/OAS documents all of the debt agreements and other documents with financial compliance requirements and develops a plan to meet all of the requirements.

Travel Advances

The Board has found that not all employees provide support for their official travel expenditures in a timely manner. OAS does not have an effective process in place to monitor this issue. In addition, there is no effective process in place to monitor the travel advances provided to contractors. OAS management is in the process of developing an automated system which it believes will assist in the oversight of this issue. However, it has not been completed.

1.21 The Board reaffirms its recommendation that GS/OAS review travel expense advances on a timely basis and also consider requiring contractors to provide travel expense support by completing appropriate forms.

Inventory Tracking

Both the external financial statement auditors and the Inspector General noted issues related to the inadequacy of OAS' inventory records. For instance, during a number of audits performed by OIG, it noted items that were not included on the inventory records as well as items that were included that were no longer owned by OAS. Although OAS has taken some steps to address this issue, it needs to continue to improve the inventory recording and reconciliation process.

1.22 The Board reaffirms its recommendation for GS/OAS to improve the reconciliation of fixed asset tracking records and the inventory accounts.

