

## **Board of the Centre**

79th Session, Turin, 27-28 October 2016

**CC 79/3/4**

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**FOR INFORMATION**

THIRD ITEM ON THE AGENDA

### **Plan for the audit of the 2016 Financial Statements**





**International Training Centre  
of the  
International Labour Organization  
AUDIT PLAN  
Financial Year 2016**



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**About the Audit Plan:**

This audit plan will guide the delivery of our audit function in the International Training Centre of the International Labour Organization for the Calendar Year 2016. This plan specifically presents our audit objectives that are based on the mandated functions; the basic audit works based on our audit approach and methodology; the audit milestones; and, the management of audit resources. This audit plan also lays out our audit trajectories based on the results of our initial audit engagement conducted in June 2016 at the start of our mandate which are bound to evolve as our audit progresses which implies that this Audit Plan is a living document.



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## **Mandate and Scope of Work**

1. The ILO Governing Body appointed the Chairperson of the Commission on Audit, Republic of the Philippines (COA), as the External Auditor of the ILO for financial years 2016 to 2019, with the appointment to commence on 1 April 2016 covering a period of four years.
2. In accordance with the Financial Regulations of the ITC of the ILO referred to this document as the Centre, the external auditor of the ILO is also the external auditor of the Centre.
3. The Centre's *Financial Regulations*, chapter IX, defines the terms of reference governing the external audit. The regulations require that the external auditor report to the Board on the audit of the financial statements of the Centre and on other such matters that should be brought to its attention.

## **Overall Audit objectives**

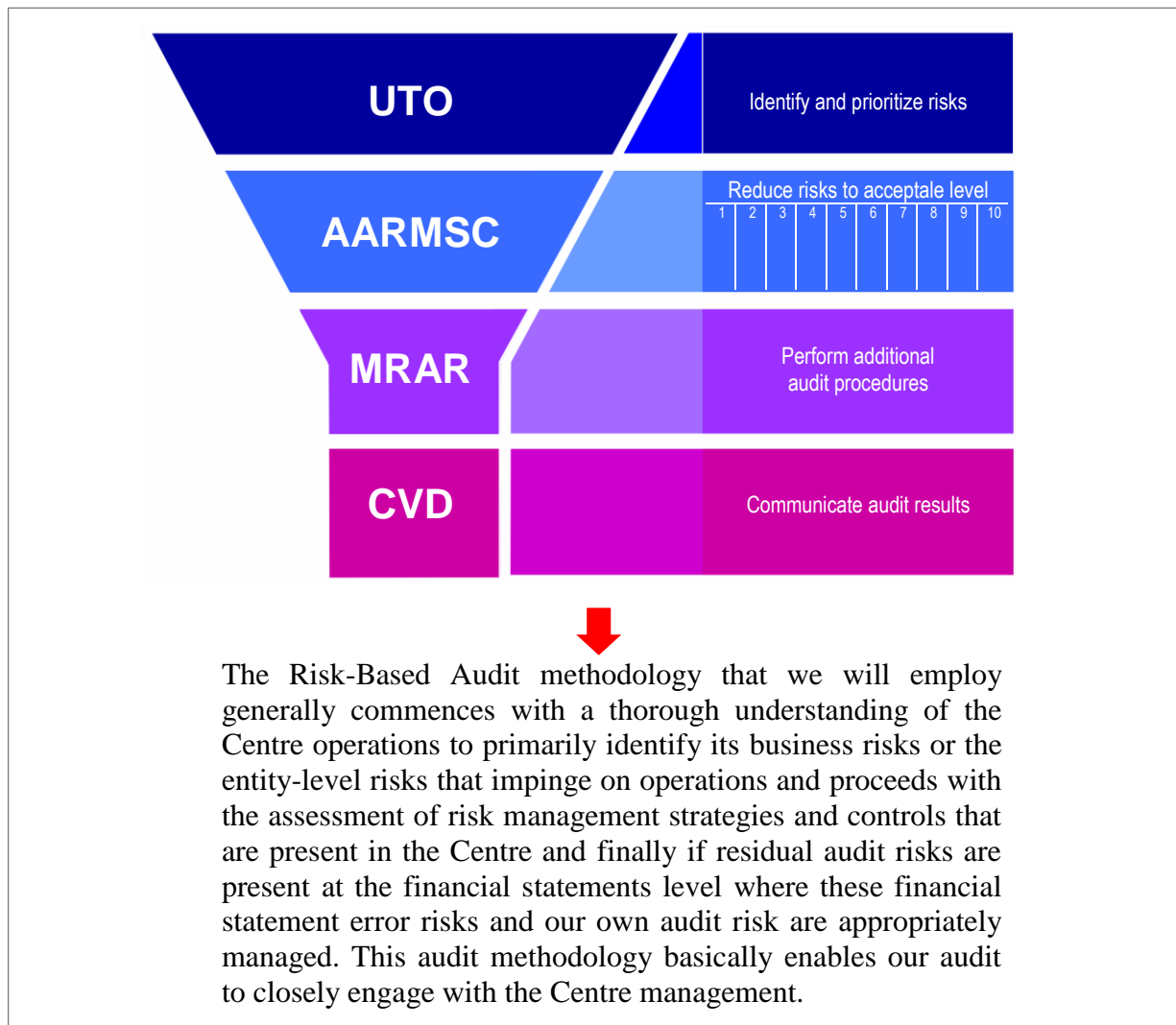
4. Our overall audit objectives are:
  - a. to express an independent opinion as to whether:
    - i. the financial statements present fairly, in all material respects, the financial position of Centre as at 31 December 2016, and the results of its financial performance, its cash flows and the comparisons of budget to actual amounts for the year then ended in accordance with International Public Sector Accounting Standards (IPSAS);
    - ii. the Centre's financial statements were prepared in accordance with the stated accounting policies;
    - iii. The accounting principles were applied on a basis consistent with that of the preceding financial period; and
    - iv. The transactions that have come to our notice during the audit of the financial statements have, in all significant respects, been made in compliance with the Centre's Financial Regulations and legislative authority.
  - b. to make observations with respect to the efficiency of the financial procedures, the accounting system, the internal financial controls and in general, the administration and management of the Centre (Chapter IX of the Financial Regulations).



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## Audit Approach and Methodology

5. In alignment to the requirements of the International Standards on Auditing (ISA), we will apply the risk-based approach in the audit of the Centre's Financial Statements as well as its operational management. The audit approach will be delivered with an audit methodology that will align our audit process more closely with the Centre's need to further enhance its governance particularly in the area of financial reporting; provide the users of its financial statements with a higher level of assurance that operational processes are designed and operating effectively; and, enable us to perform more effective and efficient audit of the Centre's accounts and resources which is aligned to its accountability goals. The risk-based audit methodology that we will employ is depicted in the diagram below:



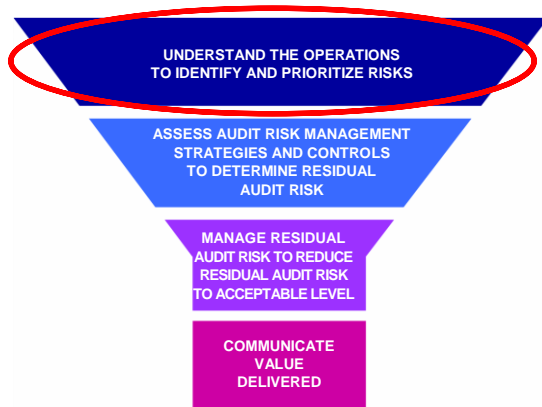
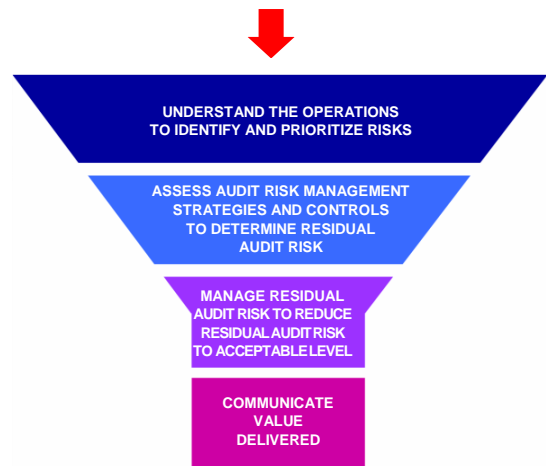


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6. In the delivery of the risk-based audit methodology, we will employ systematic and logical procedures, as follows:

**A.** The audit methodology that we utilize ensures that before undertaking field work, major entity-level risks (strategic risks) that can have an impact on our audit assignment management and other audit planning process factors such as competency and independence are identified. Further, we assess beforehand the complexity of information technology of our client and the relevance and efficiency of using the works of IT audit expert and that of the Internal Audit general described as Work of Others.

It is also at this point where we create the audit time budget and the plan to monitor time spent, conduct a planning meeting with the audit teams and prepare the “PBC” list with any analyses, confirmation letters and other documents that will be needed at the beginning of the audit field work.

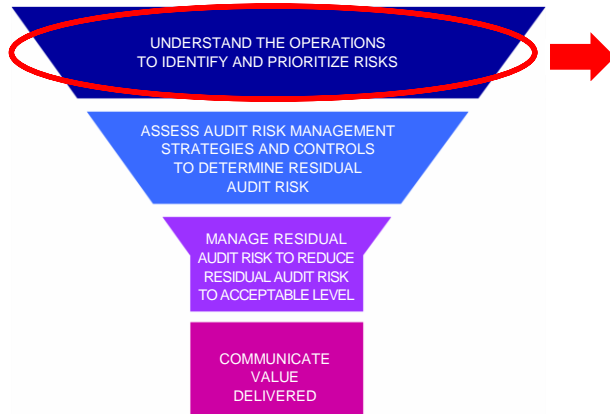


**B.** The understanding of the operations (UTO) of the Centre forms the largest part of our audit where the Centre business risks are assessed from different operational perspectives.





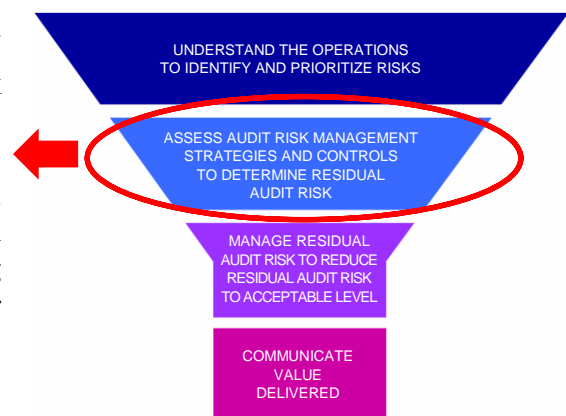
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**C.** It is in the conduct of the UTO phase of the audit where we establish the working materiality level, tolerable error and listing scopes for adjustments. In this phase, we will also perform the following procedures to identify the Centre business risks:

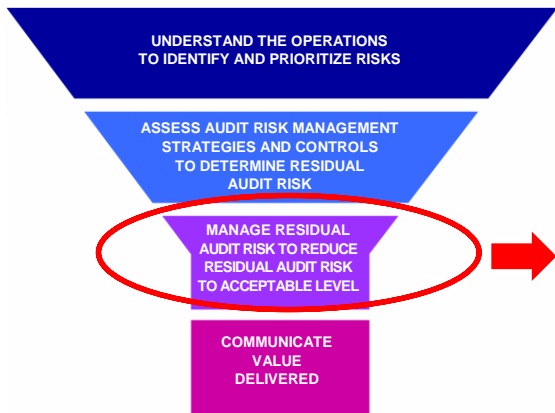
- a. The Centre's governance assessment including risk management process effectiveness assessment
- b. Fraud risk assessment which is conducted all throughout the engagement
- c. Assessment of the Centre's operational conditions, key strategic and operating success factors and entity-level risks
- d. Conduct of performance review, operational performance measures and monitoring activities
- e. Analysis of Centre's Risk Topology
- f. Risk Documentation
- g. Linking the Centre's business risks to financial statements risk including understanding of the Centre process to identify the Centre claims and assessments that may be material to financial statements including disclosures

**D.** The second phase of our audit methodology relates to the assessment of the Centre's risk management and controls pertaining to its business risks and those financial statements risk controls particularly risks of errors along the critical information, financial reporting and estimation processes. The most appropriate controls testing strategy will be applied during this phase where our audit risks are initially defined and clarified.





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**E.** The management of residual audit risk forms part of the third phase of our audit where critical financial statement risks are appropriately managed through further testing to reduce the risks to appropriately low level. It is at this point where audit response is developed for inappropriate divergence from standard practice resulting to risks of financial statement misstatement due to error or fraud. These risks can reside within the critical processes, judgments and estimates, financial reporting process including disclosures. Analytical procedures will also be performed at this juncture for low risk material accounts to comply with ISA requirement for minimum substantive procedures that must be applied to these accounts.

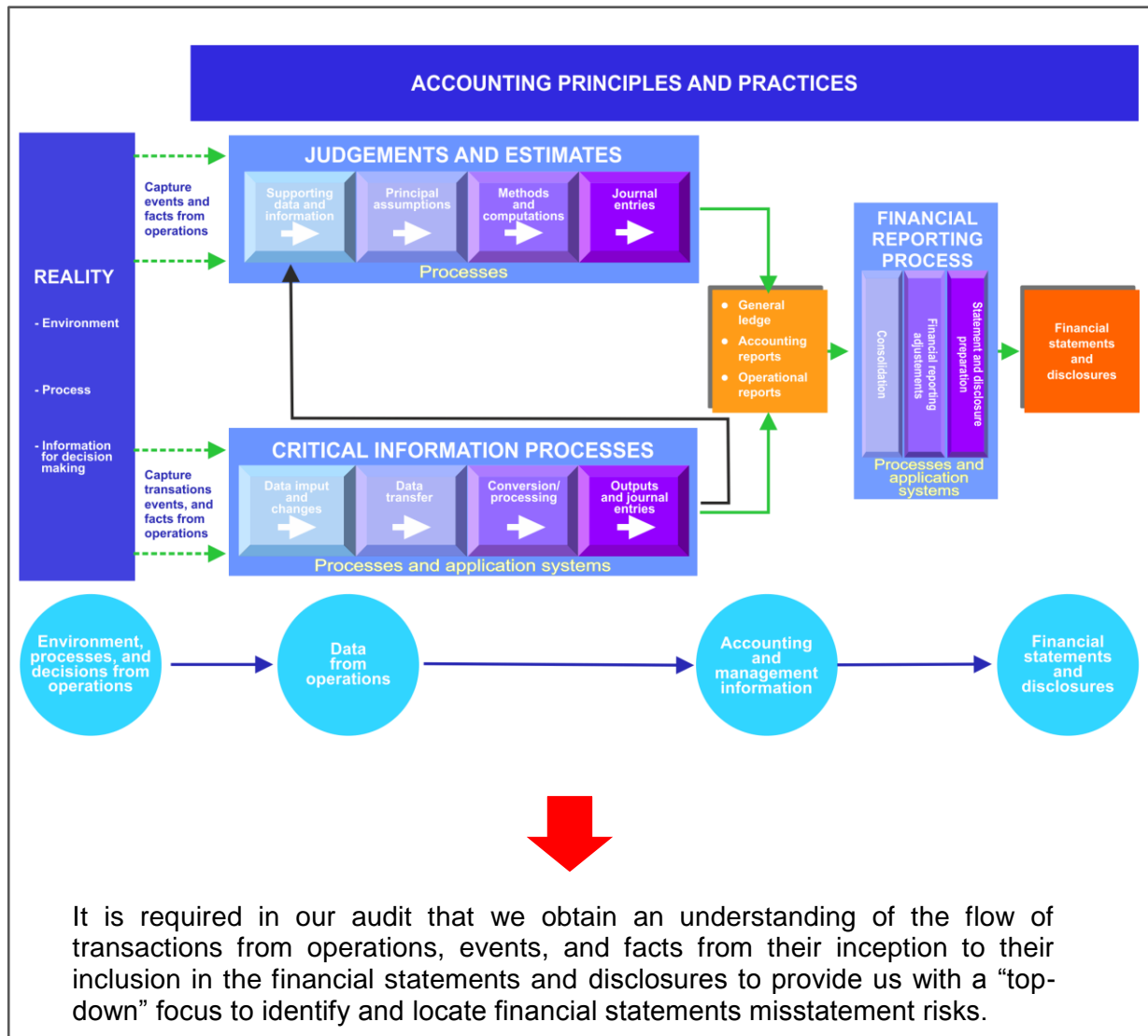
**F.** The communication of the value delivered in our audit is the last phase of our audit methodology. This phase deals with the discussion of audit findings and conclusion with the Centre's management for their resolution. While communication with management is maintained by us from the first phase of our audit, this phase is particularly material because of the nature of the audit results which basically relate to financial statements fair presentation. Overall, this phase of our audit also covers activities relating to audit and advisory report preparation and presentation.



- During the entire course of our audit, establishing information integrity occupies the foremost consideration as we carry out the probing of information provided by the Centre relating to its relevance and reliability. Consideration of information integrity is the key to the judgmental aspect of our audit process. Specifically, this information integrity principle is applied in the following diagram as the information is translated from reality up to the financial statements:



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## Initial Risk Perspectives

8. During our initial audit engagement, we determined a number of relevant factors and changes within the Centre operations that we consider as our initial audit trajectories. While our observations do not warrant that risks indeed reside in several operational aspects of the Centre’s management, we have planned to input this information into our first audit field work – first interim audit of our mandate and the succeeding year-end audit for 2016. These factors and changes presented below, will enable us to define and clarify entity-level risks commencing from the first interim audit and ultimately draw up the Centre risk topology from our audit perspective:



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## Revenue generation and Training Programme Governance

### Context

The Centre is the training arm of the International Labour Organization (ILO), a United Nations agency entrusted with promoting social justice, including internationally recognized human rights and labour standards. Thus, it provides training in subjects that further the ILO's pursuit of decent work for all and ensure that this training for the world is relevant and appropriate to local needs, aspirations and conditions.

The Centre is strongly reliant on earned income from the Training Department. In 2015, about 65% of all revenue generated by the Centre was income from training while another 30% stemmed from fixed contributions from the Government of Italy and ILO to cover running costs; another 5% income was generated from the production and sales of publications and miscellaneous. More than 40% of all income generated by the Training Department came from ILO contracts (whether signed by HQ departments, ILO field offices or ILO-led TC projects), while another 50% related to contracts signed with institutional clients or activities financed with earmarked contributions from Governments. By direct comparison, self-paying individual clients make up less than 10% of the customer universe.

Moreover, year 2015 was a break even financial positive year for the Centre whereby its total revenue was higher by 9.8 per cent as compared to its 2014 results. This was primarily due to the increase of 21% in training revenue as well as the realization of an exchange gain on the ILO contribution and increased other revenue.

### Risk Perspectives

**Revenue generation and funding.** Previous audit risk assessment revealed that the Centre continues to face funding and revenue generation challenges due to the ongoing economic climate and specialized training needs in many countries. Non-compliance with the *Financial Regulations* of the Centre is probable, if the Centre was not able to carry out certain activities with respect to its budget, the use of funds was not for the intended purpose thus, affecting the attainment of its objectives.

**Training Programmes.** Marketing/advertising of training programmes is fragmented as the function is exercised per unit or programme. The absence of an optimum marketing strategy may peril the sustainability of the training programmes.

**Publications Services.** Publications services may not be sustainable over time. This could mainly be due to inaccurate or incomplete cost estimates, mismanagement of production resources, decrease in the external demand of the services or the lack or absence of corresponding policy, among others.



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## Financial Reporting and Critical Information Processes

### Context

The financial statements of the Centre are consolidated with ILO and prepared in accordance with International Public Sector Accounting Standards (IPSAS) and the Financial Regulations. The preparation of IPSAS compliant financial statements requires management to make judgments, estimates and assumptions. Management considers assumptions and estimates on provisions for doubtful accounts and useful life of PPE as significant. We noted however, that the provisions rely on whether the probability of collections is doubtful based on information on hand at a certain time. There is little in the way of estimation as the Centre does a one-on-one analysis of each Accounts Receivable over a certain age. Regarding the useful life of PPE, the estimate is related to the useful life. We noted however IPSAS compliant financial statements are also prepared on an accrual basis. This means that transactions and events are recorded and recognized in the financial year to which they relate. This requires the Centre to perform closure activities with varying forms of complexities.

### Risk Perspectives

**Judgements and Estimates.** Accounts Receivables and PPE comprises 16% and 30% of the overall assets of the Centre as of December 31, 2015, respectively. Estimates affecting these accounts are may be considered significant and may correspond to higher risk.

The following are potentially significant estimates that represent a higher risk:

- Provision for doubtful accounts
- Useful lives of property and equipment

**Cut-off Procedures.** Transactions may not be accounted for in the appropriate financial year relating to accruals for both revenue and expenses due to the complexity of transactions in relation to the requirements of IPSAS financial reporting. This could result in inaccurate revenue and expense figures, causing misleading results.

**Purchase transactions.** This stream of transactions relates to all of the steps in the process of purchasing, including the authorization of purchases, the receipt of goods and services, and the recording of expenses, payables and payments. The following are key areas where risks can reside and may affect the fair presentation of the Financial Statements:

- Authorization for purchases: the authorization for purchasing may not be clearly defined or may not comply with the delegation of Authority of the Centre, both in terms of the types of goods and services as well as cost threshold of the procurement.
- Receipt of incorrect delivery: occurrence of different item (or quantity) delivered than what was ordered.



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- Payment for goods or services not received: error on the part of the supplier/vendor, a loss in transit, or as the result of a fictitious invoice.
- Errors in the amount paid: payments verification against the invoice before payment is not appropriate.

## Information Technology Management

### Context

Information Technology has been identified as a strategic enabler and driver of change in the strategic direction of the Centre's operations. Significant improvements had been in place in recent years that included restructuring and realigning the IT function to facilitate a Centre-wide approach to governance and management of IT resources and assets, and to establish a roadmap towards IT service excellence by delivering modern, efficient and cost-effective IT services, which are more closely aligned with the needs of the Centre's technical and financial operations. In order to respond to the paradigm shift in the world of learning and training, the Centre must continue to evaluate its training delivery models and ensure that innovations are implemented on a continuing basis. To date, several large-scale IT projects are in the pipeline which can impact the organization at an organizational level including its financial operations such as the Management of Activities and Participants (MAP) ver. 3.0, the Oracle ERP upgrade as well as the Enhancement of the Oracle procurement process.

### Risk Perspectives

**Deployment plan of the ERP upgrade.** The planned upgrade of the existing Oracle ERP E-Business Suite (EBS) version 11 to EBS 12 is not covered by a formalized Migration Plan from which all areas of the enhancement can be considered to minimize the possibility of failure, such as formally agreed security restrictions, appropriate training documentation and designed training plan, data migration policy documents, data cleansing activities and migration fall back policy. The planned upgrade could result in inaccurate migration of data from the old to the upgraded system causing misleading figures and misstatements in the financial statements.

**IT Processes for Financial Reporting.** Information / data reflected in the financial statements are produced from linkages between the manual and computerized processes. The transition from one process to another is inherently susceptible to data integrity concerns. The on-going automation or upgrade of the Oracle Application may result to efficient operations but may adversely impact the operations due to inadequate migration planning specifically on security, data cleansing, testing and migration fallback procedures.



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## Procurement Administration

### Context

The ITC financial rules enumerates the general principles of procurement:

- best value for money;
- economy and efficiency to achieve quality and cost effectiveness;
- fair and open competition giving all qualified suppliers an opportunity to participate;
- transparency and accountability in the procurement process; and
- any other interest of the Centre

On the other hand, procedural steps pertaining to the procurement are provided through Circulars issued by Financial Services and Human Resources Services. Informal or formal bidding procedures are carried out depending on the value of the procurement transaction.

It was observed, however, that this process is very much decentralized to each unit other than for large purchases of service contracts for the Campus maintenance and hotel/cafeteria/bus services.

### Risk Perspectives

**Best value for money in procurement.** Failure to follow effective evaluation procedures for offers may increase the risk of inconsistent evaluations and may result in non-attainment of value for money.

**Vendor management policy.** Procurement, as a major activity, involves transactions with simple to varied and complex requirements. Currently, FINSERV 04/2014 and HRS 11/2012 covers the procedures for the procurement of goods / services and external collaboration contracts, respectively. Both Circulars were unclear on the management of vendor / supplier and evaluation criteria and may not result in attainment of value for money.





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## Audit Materiality

9. Our audit requires us to determine a specific amount of materiality for each engagement. This amount is also used to evaluate the significance of uncorrected misstatements (*past* adjustments and reclassifications) noted during the audit. Our initial working materiality is presented below:

	Basis	Amount
Overall Materiality	2% of the average total expenses of the Centre from the last two biennia	€759,710
Unadjusted and adjusted items in excess of this amount will be reported to the management	5% of over-all materiality	€37,986

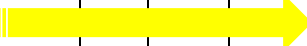




10. We considered the following factors in establishing materiality: the needs of the Centre and other contributors, representatives of governments, employers and workers and other multilateral agencies. This is consistent with the materiality level used for the 2015 financial statement audit of our predecessor. However, the quantitative measure of materiality is not the only factor considered in evaluating misstatements. Relatively small misstatements may have material effect on the financial statements because of qualitative considerations. The Centre will be given an update on the final determination of materiality.





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## Planned Works

Activities	Month											
	2016							2017				
	Jun	Jul	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May
<b>Audit Assignment Risk Assessment and Management</b> - Assessment of major risk indicators - Assessment of need/use of Work of Others - Create time budget/planning meeting												
<b>Understand Auditee Operations</b> - Risk Management Process and Fraud Risk Assessment - Operations analysis and performance review - Analysis of critical information processes including financial reporting - Financial Statements linkage determination - Review of PBCs												
<b>Assess Risk Management and Controls</b> - Assess risk management strategies and controls to reduce												



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Activities	Month											
	2016							2017				
	Jun	Jul	Aug	Sept	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May
risk to an acceptable level (entity-level and process level risks)												
<b>Manage Residual Audit Risk</b> <ul style="list-style-type: none"> <li>- Respond to identified FS error risks</li> <li>- Perform substantive audit tests/confirmations</li> <li>- Perform analytical procedures on low risk material accounts</li> <li>- Overall review of FS for reasonableness</li> <li>- Perform subsequent review procedures</li> </ul>												
<b>Communicate Value Delivered</b> <ul style="list-style-type: none"> <li>- Issuance of Audit Observation Memorandum</li> <li>- Issuance of Management Letters</li> <li>- Issuance of Audit Report/Long Form Report</li> <li>- Presentation of Audit Report to the Board</li> </ul>												

In the Philippines

In ITC



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### Significant Audit Deliverables

- a. At the conclusion of the audit, we will provide the following reports:
- **Independent Auditor's Report.** This is a signed opinion on the financial statements as at 31 December 2016; and
  - **Report of the External Auditor to the Board.** This will contain our findings with respect to the efficiency of the financial procedures, the accounting system, financial controls and, in general, the administration and management of the Centre, and all matters referred to in Chapter IX, Article 25 of the Financial Regulations. We will provide an update on prior years' observations and the implementation of recommendations. It will also contain the current year's observations and recommendations.
- b. In addition, we will provide management with the following reports during the course of our audit:
- **Management letter.** A derivative communication that identifies opportunities for changes in procedures that would improve systems of internal control, streamline operations, and/or enhance financial reporting practices.
  - **Audit Observation Memoranda.** A written communication to concerned staff and official informing them of the deficiencies observed in the audit of accounts, operations or transactions.

### Significant Audit Milestones

Activity	Date
Initial audit engagement	June 2016
Presentation of Audit Plan	26-28 October 2016
First Interim Audit	24 October to 16 November 2016
Year-end Audit	13 February to 08 March 2017
Signed Audit Opinion	3 <sup>rd</sup> week March 2017
Presentation of Audit Results to Governing Body	May 2017



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### Other Audit Services

As the Centre's external auditor, we expect to perform audits based on requests by the Centre's donors. Separate Terms of Engagement will be prepared thereof.

### Planned Field Works

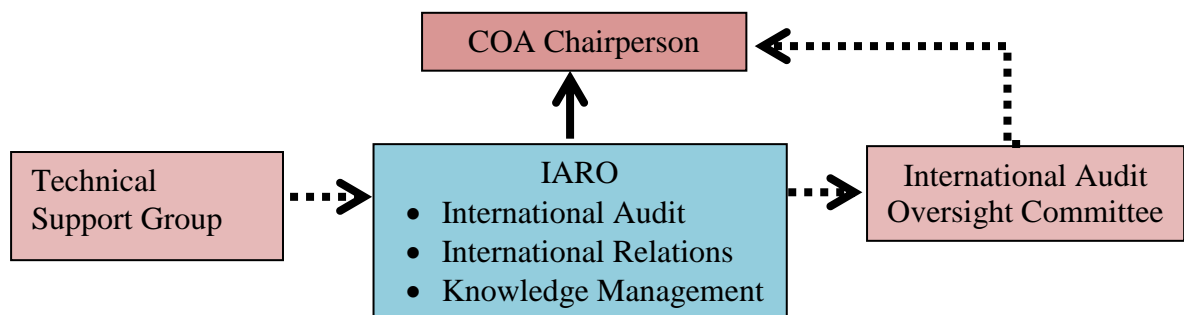
Offices to be visited/ Tentative Date	Audit Areas	No. of Audit Personnel	Audit Output
<b>Interim audit ITC of the ILO</b> 24 October to 16 November 2016	Financial Audit: Review of financial reporting process; proforma financial statements and disclosures; substantive tests of transactions from January to September 2016	3	Management Letter
<b>ITC of the ILO</b> 13 February to 8 March 2017	<b>Year-end Financial Audit:</b> Audit of Financial Statements, note disclosures and schedules as at 31 December 2016  Test of balances and substantive tests of transactions for 2016	3	Management Letter Independent Auditor's Report Long Form Report



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## Audit Management

11. The management of our audits is based on our established operating philosophy of aligning our audit process more closely with the needs of its international clientele to improve its governance and provide the users of its financial statements with a higher level of assurance that our client's processes are effective as to their design and operation. To this end, we have created the International Audit and Relations Office (IARO) to serve as the main focal point in the management of our international commitments.
12. The governance structure of the IARO is presented below:



13. The audit of the Centre will be performed by a team composed of experienced professional auditors from the Commission on Audit solely dedicated in the audit of the Centre. Effective manning strategies are adopted in the deployment of the auditors that include effective skills mixing, bespoke technical trainings and adequate support mechanisms.
14. To ensure audit quality, we abide the ISA standards on audit quality. Our audits undergo a three-level review commencing with the Director of IARO and assisted by the Technical Support Group. The second level review emanates from the International Audit Oversight Committee the performs a set of quality assurance procedures to ensure that audit information and reports are of a high level of integrity before these are escalated to the third and final level of review. The Chairperson, Commission on Audit, Philippines performs the final review of our outputs and is also consulted on sensitive, complex, and/or difficult issues.
15. The principal and senior staff involved in the audit of the ITC of the ILO are as follows:
- |                      |   |
|----------------------|---|
| a. Michael Aguinaldo | Chairperson, Commission on Audit, Philippines |
| b. Lito Martin       | Director, External Audit (IARO)               |
| c. Danilo Cabug      | Deputy Director, External Audit (IARO)        |