



International Oil Pollution
Compensation Funds

Agenda Item 6	IOPC/OCT19/6/1	
Date	5 September 2019	
Original	English	
1992 Fund Assembly	92A24	●
1992 Fund Executive Committee	92EC73	
Supplementary Fund Assembly	SA16	●

APPOINTMENT OF THE EXTERNAL AUDITOR

2020 ACCOUNTING YEAR

Note by the Audit Body

Summary:

The current term of the External Auditor, BDO International (BDO), covers the financial years 2016–2019. As a result, their period of office will end following their report on the 2019 Financial Statements at the 2020 regular sessions of the governing bodies. The management of the selection process of the External Auditor falls within the mandate of the Audit Body.

At the April 2019 sessions of the governing bodies, the Audit Body outlined the various options for appointing an External Auditor for a period commencing with the 2020 financial year (see document IOPC/APR19/6/1). The governing bodies expressed support for the recommendation made by the Audit Body to conduct a formal review and evaluation of BDO's performance and their proposals for a further term. The governing bodies also supported the Audit Body's offer to make a recommendation to them on this matter at their October 2019 sessions. In addition, the governing bodies suggested that the Audit Body develop clear rules for the appointment of the External Auditor for the future (see document IOPC/APR19/9/1, paragraph 6.1.6).

At its meeting held on 21 June 2019, the Audit Body conducted a formal review and interview session with BDO as a result of which it recommends that BDO be re-appointed as the IOPC Funds' External Auditor for a second four-year term, subject to continuing satisfactory performance, commencing with the 2020 financial year.

As requested by the governing bodies, the Audit Body also submits a proposal on the possible selection process of future External Auditors to the governing bodies for their consideration (see section 3).

Action to be taken:

1992 Fund Assembly and Supplementary Fund Assembly

- (a) decide whether to follow the Audit Body's recommendation that BDO be re-appointed as the IOPC Funds' External Auditor to audit the Financial Statements of the 1992 Fund and the Supplementary Fund for a second four-year term, i.e. the financial years 2020–2023 inclusive, subject to continuing satisfactory performance;
- (b) decide whether to approve the selection process of the External Auditor for the future as proposed by the Audit Body and detailed under paragraphs 3.3 to 3.5; and, if so,

- (c) decide whether to amend Financial Regulation 14 of the 1992 Fund and the Supplementary Fund as set out in paragraph 3.6.

1 Introduction

- 1.1 The current term of the External Auditor, BDO International (BDO), covers the financial years 2016–2019. As a result, their period of office will end following their report on the 2019 Financial Statements at the 2020 regular sessions of the governing bodies.
- 1.2 This issue falls within the Audit Body mandate which states that the Audit Body shall ‘manage the process for the selection of the External Auditor’.
- 1.3 At the April 2019 sessions of the governing bodies, the Audit Body outlined the various options for appointing an External Auditor for a period commencing with the 2020 financial year (see document IOPC/APR19/6/1). The 1992 Fund Administrative Council and Supplementary Fund Assembly requested the Audit Body to:
- (a) conduct a formal review of the current External Auditor, BDO, including an assessment of their performance and their proposals for a further term, including fees; and
 - (b) following the review, to make a recommendation to the governing bodies at their October 2019 sessions as to whether the current External Auditor should be re-appointed for a further term or whether a full tender process should be undertaken.
- 1.4 In addition, and, following the suggestion of one delegation, which was supported by a number of other delegations, the Audit Body also stated that it would propose clear rules on how to conduct the selection of future External Auditors.

2 Review process and recommendation

- 2.1 The process involved inviting BDO for a formal review and interview session with the Audit Body (as well as with members of the Secretariat and the 1992 Fund Assembly Chair in attendance as invitees) to coincide with the Audit Body meeting held on 21 June 2019. Apologies for absence were received from the Chair of the Supplementary Fund Assembly, Mr Sung-Bum Kim, who could not attend the meeting.
- 2.2 The review covered the following:
- (a) review of service to date with emphasis on value delivered and any lessons to be learned;
 - (b) proposal for ensuring continuity of key team members and associated structure in order to
 - (c) safeguard audit quality and service;
 - (d) audit approach proposals;
 - (e) assessment of future challenges facing the IOPC Funds and BDO observations; and
 - (f) fee proposals.
- 2.3 The process was similar to that followed in the 2015 tender process whereby the External Auditor had prepared a written proposal setting out their credentials and service commitment for a further term, followed by a structured interview. The Audit Body also had the benefit of a document, prepared by the Secretariat, setting out their views on the service provided by BDO to date.

2.4 The principal matters that arose from BDO's presentation and the questions posed by the Audit Body were as follows:

- BDO had effected a smooth handover and transition of responsibilities from the previous External Auditor and had put in place a good team who had provided reasonable continuity to date;
- BDO had gained a good understanding of the work of the IOPC Funds and had developed effective working relationships with key members of the Secretariat while being robust in carrying out the work. BDO had also demonstrated a sound appreciation of the challenges facing the IOPC Funds in the future;
- BDO had provided constructive advice alongside their primary responsibilities regarding the audit of the Financial Statements;
- BDO had adhered to all reporting deadlines, and their reports were clear and relevant;
- As stated below, BDO had proposed a total fee of £58 000, fixed for the four years commencing in 2020, compared with the current fee of £46 400, fixed in 2016:

	2016–2019 (£)	2020–2023 (£)
1992 Fund	43 200	53 600
Supplementary Fund	3 200	4 400
Total	46 400	58 000

- The rate increase was the result of salary pressures and a slight increase in resources. The Audit Body discussed this with both BDO and the Secretariat and was satisfied the proposal was reasonable and represented value for money; and
- BDO had committed to ensuring continuity at the partner level for the second term and had also planned for continuity at the manager level.

2.5 Taking into account the above-mentioned points and given BDO's commitment to serving the IOPC Funds as a valued client, the Audit Body recommends that BDO be re-appointed as the IOPC Funds' External Auditor for a second four-year term, subject to continuing satisfactory performance, commencing with the 2020 financial year.

3 Selection process of External Auditors in the future

3.1 In addition to the current review covering a four-year term commencing with the 2020 financial year, the Audit Body has also considered the rules to be established for the future selection process of the External Auditor. In this regard, the three basic options, i.e. a full tender; a formal review; and the straightforward re-appointment of the incumbent External Auditor, have been outlined in document IOPC/APR19/6/1. Going forward, the Audit Body considers that straightforward re-appointment of an External Auditor for a four-year term is inconsistent with best practice, and this option is therefore discounted.

3.2 Thus, the issue becomes that of considering the respective merits of conducting a full tender or a formal review. The previously identified advantages and drawbacks of the relevant options can be summarised as follows:

A full tender

- (a) Rebuttable presumption that a tender ensures value for money is obtained, although any headline monetary savings are offset against the costs of disruption to the Secretariat from the tender process and the process of transition to a new External Auditor;

- (b) Costly and time-consuming for audit organisations which can result in the reduction of the number of bidders if the process is repeated frequently;
- (c) Inconsistent with best practice where changes of auditors after a short period are not considered to be practical or efficient; and
- (d) It becomes necessary, after a prolonged period with an incumbent auditor, to effect a rotation in accordance with best practice.

A formal review of the incumbent

- (a) Provides a blend of the advantages of the other options in that it combines economy with the need to obtain value for money;
- (b) A process consistent with the situation where there is satisfaction with the service provided by the incumbent in terms of independence, rigour and a competitive fee;
- (c) Consistent with current corporate governance best practice where the auditor has not served for an extended period; and
- (d) If the outcome of a review were to be unsatisfactory, there should remain sufficient time and scope to conduct a full tender process.

- 3.3 Having considered the above, the Audit Body is of the view that there is merit in both options and recommends that, subject to certain conditions being met, there should be an alternation between a full tender and a formal review at the end of each four-year period of tenure. This presumes that, for a formal review to be conducted, there is overall satisfaction with the quality of service being provided by the incumbent and that they are prepared to serve for a further term. If these conditions were not met, a full tender would be held. The alternation between a full tender and a formal review would total eight years, which is consistent with best practice. With a change in auditor, a new eight-year cycle would commence.
- 3.4 The next issue to consider is whether it is appropriate that an incumbent External Auditor who has served for two four-year terms be eligible for appointment for a further term. Examination of practice elsewhere indicates there is a considerable range of possibilities: certain organisations have a limit close to eight years, whereas in the European Union, for example, the limit for public interest entities is 20 years before a change of auditor is required subject to there being a tender after 10 years.
- 3.5 Bearing in mind that all commercial audit firms have strict rules on partner rotation to minimise the risk of loss of independence, the Audit Body considers there is a sound case for a change in audit organisation following a full tender after two terms of four years. However, the re-appointment for one further term of the incumbent who has already served for two four-year terms should not be ruled out. In such circumstances, it would be for the governing bodies to decide whether such re-appointment should be for four years or a shorter period.
- 3.6 Should the governing bodies approve the selection process of the External Auditor proposed by the Audit Body as detailed under paragraphs 3.3 to 3.5, Financial Regulation 14 of the 1992 Fund and the Supplementary Fund would need to be amended as follows:

Current text	New text (proposal)
<p style="text-align: center;">Financial Regulation 14^{<1>}</p> <p style="text-align: center;">External Audit</p> <p>14.1 An External Auditor, who shall be the Auditor-General (or officer holding the equivalent title) of a Member State, or a commercial firm with the requisite capabilities nominated by a Member State or identified by the Audit Body, shall be appointed in the manner and for the period decided by the Assembly.</p>	<p style="text-align: center;">Financial Regulation 14^{<1>}</p> <p style="text-align: center;">External Audit</p> <p>14.1 An External Auditor, who shall be the Auditor-General (or officer holding the equivalent title) of a Member State, or a commercial firm with the requisite capabilities nominated by a Member State or identified by the Audit Body, shall be appointed in the manner and for the period decided by the Assembly. <u>Ordinarily, such appointment will be for four years and be the result of a tender process conducted by the Audit Body and its subsequent recommendation to the Assembly.</u></p> <p><u>Depending on satisfactory performance, the initial appointment may be extended for a further period of up to four years. The External Auditor may serve for another period if the Audit Body after undertaking an objective assessment of the qualifications and performances of the incumbent External Auditor recommends to the Assembly an extension of the term of appointment. After serving as an External Auditor for two consecutive periods, the appointment of the External Auditor may, in exceptional circumstances, be extended as a result of a full tender process. The Assembly decides on the manner and the period applicable to such an extension based on a recommendation by the Audit Body.</u></p>

4 Recommendation by the Audit Body

- 4.1 Taking into account the result of the formal review and the interview of BDO, the Audit Body recommends that BDO be re-appointed for a further four-year term commencing with the 2020 financial year.
- 4.2 The Audit Body also recommends that Financial Regulation 14 be amended accordingly to reflect the proposed selection process of the External Auditor as detailed in paragraphs 3.3 to 3.5.

^{<1>} Financial Regulation 14.1 of the Supplementary Fund differs slightly to that of the 1992 Fund in that it specifies that the External Auditor shall be the Auditor-General of a 1992 Fund Member State. In all other instances the text is identical.

5 Action to be taken

1992 Fund Assembly and Supplementary Fund Assembly

The 1992 Fund Assembly and the Supplementary Fund Assembly are invited to:

- (a) decide whether to follow the Audit Body's recommendation that BDO be re-appointed as the IOPC Funds' External Auditor to audit the Financial Statements of the 1992 Fund and the Supplementary Fund for a second four-year term, i.e. the financial years 2020–2023 inclusive, subject to continuing satisfactory performance;
 - (b) decide whether to approve the selection process of the External Auditor for the future as proposed by the Audit Body and detailed under paragraphs 3.3 to 3.5; and, if so,
 - (c) decide whether to amend Financial Regulation 14 of the 1992 Fund and the Supplementary Fund as set out in paragraph 3.6.
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