



INTERNATIONAL
OIL POLLUTION
COMPENSATION
FUNDS 1971 AND
1992

ASSEMBLY
6th extraordinary session
Agenda item 4

92FUND/A/ES.6/3
19 March 2002
Original: ENGLISH

ASSEMBLY
9th extraordinary session
Agenda item 5

71FUND/A/ES.9/3

AUDIT PROCEDURES

Note by the Director

Summary:	The governing bodies decided at their October 2001 sessions to create a joint Audit Body for the 1992 Fund and the 1971 Fund. The governing bodies decided to postpone to their next sessions the consideration of the composition and mandate of the Audit Body.
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Action to be taken:	Determine the composition and mandate of the Audit Body.
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1 **Introduction**

- 1.1 At their October 2001 sessions the 1992 Fund Assembly and the 1971 Fund Administrative Council, acting on behalf of the 1971 Fund Assembly, examined a document submitted by the Director (document 92FUND/A.6/10 and 71FUND/A.24/9) in which the governing bodies were invited to consider whether, in the interest of good management and to promote best practice in financial management and internal control, the IOPC Funds should establish an audit body to provide advice to the Director and the Assemblies in relation to internal control, risk management and audit-related matters. That document is reproduced in the Appendix to the present document.
- 1.2 Under the Director's proposal, the Audit Body would be composed of five members, for example a Chairman with knowledge and interest in management and financial matters, three persons elected from delegations of Member States and one outside member with expertise in financial matters, for example in insurance.

2 **Consideration by the governing bodies in October 2001**

- 2.1 At their October 2001 sessions, the governing bodies took the view that, since the IOPC Funds held significant assets and made compensation payments totalling high amounts, they should ensure maximum transparency in their operations. It was also considered that such a body would enable Member States to have a broader involvement in Fund matters. It was decided therefore to

create a joint Audit Body for the 1992 Fund and the 1971 Fund (documents 92FUND/A.6/28, paragraph 12.5 and 71FUND/AC.6/A.24/22, paragraph 11.6).

- 2.2 During the discussions, it was suggested that the number of members of the audit body proposed by the Director was too low, and a figure of seven rather than five was mentioned. Some delegations considered that the members of the Audit Body should reflect the geographical distribution of Member States. Other delegations suggested appointing members on a rotation basis for a term of four years, non-renewable.
- 2.3 Some delegations suggested that it could be left to governments to appoint the member for their State, whilst others considered that members should be appointed in their personal capacity according to their expertise.
- 2.4 It was emphasised that the Audit Body should not control or duplicate the External Auditor's work and should not affect the independence of the External Auditor. It was also suggested that the members of the Audit Body should be independent and should not take instructions from their Governments. The point was made that the Audit Body should not impinge on the Director's general authority as regards the operation of the IOPC Funds. It was also suggested that the Audit Body's role should not be restricted to purely financial matters but should cover also the efficiency of the Secretariat.
- 2.5 The question arose as to whether the expenses incurred by Audit Body members would be paid by the Funds. Several delegations stated that the Funds should not pay travel expenses and that it should be for the Governments to cover such expenses. Other delegations considered that unless the Funds paid these expenses this would restrict the membership.
- 2.6 The governing bodies decided to postpone to later sessions consideration of the composition and mandate of the Audit Body.

3 Mandate of the Audit Body

- 3.1 In their consideration of the composition of the Audit Body the Assemblies may recall that the Director had proposed that the Audit Body should be composed of, in addition to members elected from delegations of Member States, a Chairman with knowledge and interest in management and financial matters and one outside member with experience in financial matters.
- 3.2 The Annex to document 92FUND/A.6/10 and 71FUND/A.24/9 contained a draft mandate for the proposed audit body. The Director has reviewed this draft in the light of the discussions at the October 2001 sessions. A revised proposed mandate is at the Annex to the present document.

4 Action to be taken by the Assemblies

The Assemblies are invited:

- (a) to take note of the information contained in this document;
- (b) to determine the composition of the Audit Body and elect its members; and
- (c) to determine the mandate of the Audit Body.

APPENDIX

INTERNATIONAL OIL POLLUTION COMPENSATION FUND 1992

ASSEMBLY
6th session
Agenda item 12

92FUND/A.6/10
10 September 2001
Original: ENGLISH

ASSEMBLY
24th session
Agenda item 11

71FUND/A.24/9

AUDIT PROCEDURES

Note by the Director

Summary:	The Director invites the Assembly to consider whether, in the interest of good management and to promote best practice in financial management and internal control, the IOPC Funds should establish an audit body to provide advice to the Director and the Assemblies in relation to internal control, risk management and audit-related matters.
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Action to be taken:	Consider whether to establish such a body.
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1 Introduction

- 1.1 At its 2nd extraordinary session, held in June 1996, the 1971 Fund Assembly considered a proposal by the Chairman that the 1971 Fund should establish an Audit Committee in order to strengthen the involvement of Member States in the monitoring of the operations of the Organisations and to increase the transparency of the latter (document 71FUND/A/ES.2/21/1).
- 1.2 Under the Chairman's proposal, the Audit Committee would meet with the External Auditor before the audit of the accounts for a given year commences to discuss the priorities and special areas to be dealt with by the audit. The Committee might, for example, propose that the audit should cover not only the financial operations but also certain aspects of the Fund's management (performance audit). The Audit Committee could meet again with the External Auditor when the audit had been completed, to obtain a more detailed oral presentation of the audit than was possible at the session of the Assembly.
- 1.3 Although many delegations supported the Chairman's proposal, a number of delegations questioned the need for an Audit Committee. The issue of the establishment of an Audit Committee was on the agenda of the 19th and 20th sessions of the 1971 Fund Assembly held in 1996 and 1997 respectively, but was not considered further (documents 71FUND/A.19/7 and 71FUND/A.20/8).

- 1.4 At its 1st extraordinary session held in October 1996, the 1992 Fund Assembly decided that it was premature to consider the establishment of an Audit Committee for the 1992 Fund (document 92FUND/A.ES.1/22, paragraph 4.2). The matter has not been considered further by the 1992 Fund Assembly.

2 Renewed initiative by the External Auditor

In February 2001 the External Auditor, the Auditor and Comptroller General of the United Kingdom, raised again the issue of the establishment of a special body to deal with audit matters. The External Auditor informed the Director and the Chairman of the 1992 Fund Assembly of the developments which had taken place since the issue was considered in 1997 as set out below:

The importance of good corporate governance, including the role of the Audit Committee, has continued to develop. Best practice in the private sector has progressed with the introduction of the Stock Exchange's 'Combined Code' and the publication of 'Internal Control Guidance for Directors on the Combined Code' (the 'Turnbull Report'), which examines how specific requirements within the Combined Code should be implemented.

The Turnbull Report in particular emphasised the need for sound systems of internal control and the responsibility of the Directors to review all controls, including financial, operational and compliance controls and risk management. The Turnbull report states that a sound system of internal control 'depends on a thorough and regular evaluation of the nature and extent of the risks to which the company is exposed' and underlines the role of an Audit Committee in such processes.

There is a misconception that all members of an Audit Committee should have a financial background or expertise. In a recent publication from the Institute of Chartered Accountants of England & Wales - '*The Effective Audit Committee: a Challenging Role*' - it is stated that 'Essentials for an audit committee member are common sense, wide experience, independence, good judgement, and an understanding of the role of the audit committee and that too much emphasis on financial literacy may distract from these essentials, and that all members of the committee cannot be expected to have detailed knowledge of financial reporting standards'.

In order to provide an efficient and effective modern audit, external auditors seek where possible to rely on internal management controls and processes, where they are shown to be sound and operating. An Audit Committee can act as an effective integral part of that process.

In accordance with the 1971 and 1992 Fund Conventions, the Funds' Director is responsible for the administration of the Funds, including proper administration of the Funds' assets and preparation of financial statements. An Audit Committee should be appointed to give advice to the Director so as to assist him in meeting his internal control responsibilities.

3 Director's considerations

- 3.1 The 1971 Fund and 1992 Fund hold significant assets and make compensation payments totalling high amounts. For this reason the Director believes that the IOPC Funds should ensure maximum transparency in their operations. The discussion in the Assemblies of the report of the External Auditor can only be general and limited by time constraints.

- 3.2 The Director invites the Assemblies to renew their consideration of whether the IOPC Funds should establish a body whose mandate would be to provide advice to the Director and to the Organisations on internal control, risk management and audit-related matters, and to assist the External Auditor in performing his task.
- 3.3 In the Director's view, the proposed body should neither duplicate nor control the work of the External Auditor, who would continue to carry out his role with total independence. The body should be advisory and its members should not duplicate the work of the Secretariat or have executive functions in the day-to-day management of the Organisations.
- 3.4 The Director sees the role of the proposed body as follows:
- The audit body should promote the understanding and effectiveness of the audit within the Organisation, provide a forum to discuss internal control issues including matters raised by the audit and assist in the co-ordination of risk management, audit and any other consultancy and inspection reviews.
- Before the External Auditor begins his work, the body would be informed of the details of the envisaged work programme and, if appropriate, would make suggestions for modifications. It is nevertheless clear that the External Auditor would finally adopt his programme in complete independence. After the External Auditor has finished his audit, the body would be informed of the Auditor's observations in a more detailed presentation than can be given during the Assembly session. The body could meet twice a year, the first time in October or November to consider the External Auditor's work programme for the forthcoming audit, and a second time, in June, to consider and discuss the observations of the Auditor as a result of his audit relating to the preceding financial year. The body could also meet at the request of the External Auditor, its Chairman or the Director.
- 3.5 The Director considers that it would be useful to have a single audit body for the two Funds. The audit body could consist of five members, for example a Chairman with knowledge and interest in management and financial matters, three persons elected from delegations of Member States and one outside member with expertise in financial matters, for example in insurance.
- 3.6 The members of the audit body should be elected in their personal capacity. The individuals elected should have a good knowledge of the functioning of the IOPC Funds and have a personal interest in management and financial matters. The members of the audit body would not be entitled to send substitutes to its meetings.
- 3.7 The External Auditor, as well as the Director and the Head of the Finance and Administration Department, should attend the meetings of the audit body.
- 3.8 A draft mandate for the proposed audit body is at the Annex.

4 Action to be taken by the Assemblies

The Assemblies are invited:

- (a) to take note of the information contained in this document;
- (b) to consider the establishment of a body for the purposes set out above; and
- (c) if the Assemblies were to decide to establish such a body, to determine its mandate.

DRAFT

Mandate of the IOPC Funds' Audit Body

- 1 The Audit Body of the IOPC Funds is composed of [five] members appointed by the Assembly.
 - 2 The Audit Body should monitor the IOPC Funds' activities regarding key issues of financial reporting, internal controls and management and advise the Director and the Assemblies on these matters.
 - 3 The mandate of the Audit Body is:
 - (a) to discuss with the External Auditor the nature and scope of each forthcoming audit;
 - (b) to review the 1992 and 1971 Funds' financial statements and reports;
 - (c) to consider all relevant reports by the External Auditor, including reports on the 1992 and 1971 Funds' financial statements;
 - (d) to review the effectiveness of the 1992 and 1971 Funds' internal control system;
 - (e) to make appropriate recommendations to the respective Assemblies.
 - 4 The Audit Body should normally meet twice a year. The meetings should be convened by the Director.
 - 5 The External Auditor and Chairman of the body may request that additional meetings of the Committee should be held.
 - 6 The External Auditor, the Director and the Head of the Finance and Administration Department should be present at the meetings.
 - 7 The Chairman of the body should report on its work to each regular session of the respective Assemblies.
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ANNEX

REVISED DRAFT

Mandate of the IOPC Funds' Audit Body

- 1 The Audit Body of the IOPC Funds is composed of [xx] members appointed by the Assembly.
 - 2 The Audit Body should monitor the IOPC Funds' activities regarding key issues of financial reporting, internal controls and risk management and advise the Director and the Assemblies on these matters. It should promote the understanding and effectiveness of audit within the Organisations, and provide a forum to discuss internal control issues, operational procedures and matters raised by the external audit.
 - 3 The mandate of the Audit Body is:
 - (f) to discuss with the External Auditor the nature and scope of each forthcoming audit;
 - (g) to review the 1992 and 1971 Funds' financial statements and reports;
 - (h) to consider all relevant reports by the External Auditor, including reports on the 1992 and 1971 Funds' financial statements;
 - (i) to review the effectiveness of the 1992 and 1971 Funds' internal control system and operational procedures;
 - (j) to make appropriate recommendations to the respective Assemblies.
 - 4 The Audit Body should normally meet at least twice a year. The External Auditor and Chairman of the Audit Body may request that additional meetings should be held. The meetings should be convened by the Director.
 - 5 The External Auditor, the Director and the Head of the Finance and Administration Department should be present at the meetings.
 - 6 The Chairman of the Audit Body should report on its work to each regular session of the respective Assemblies.
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